MINORITY REPORT – SENATOR KERNOT

Towards a National Retirement Incomes Policy

The superannuation legislation before the Committee has evoked a very strong public debate and a huge amount of media interest. The Democrats regard this as a very healthy process and a vindication of the important reviewing role of the Senate.

Although there were a variety of views both for and against the legislation, there is one common thread binding the evidence given to the Committee. This thread is that all groups in the community want to have a comprehensive retirement incomes policy agreed to and enacted by the Commonwealth Parliament. The community is tired of an environment of uncertainty. People want to be able to plan knowing the rules will not be constantly changed.

This is a great step forward and offers real hope of a rational and generally accepted retirement incomes policy.

I wish to stress that the Democrats support a national, portable superannuation system.We believe that such a system, which is totally integrated with the age pension and social security system is the superior superannuation model.The system in Singapore is without parallel in respect of simplicity, flexibility and popularity with its members.

Such a system would simplify greatly the current complexity by ensuring that everybody was a member of the same fund, that everybody obtained the same benefit for equal contributions, that superannuation is an addition to a minimum pension benefit, that employers and employees only have to deal with one organisation on all superannuation matters, that the exploitation of some superannuation fund members by unscrupulous people is eliminated, that the total amount of superannuation devoted to administration and other charges and fees is substantially reduced, that the money invested in superannuation be used to strengthen local industry and employment, and probably most importantly that the funds would then be guaranteed by the Government.

Unfortunately, despite repeated attempts to convince the Government and the Opposition to support such an approach there is no chance of such a national system being implemented.

Instead the Government has proposed that the Superannuation Guarantee Levy system be introduced.

The Superannuation Guarantee Levy (SGL) Proposal

The SGL legislation proposes to achieve two distinct objectives: to increase the coverage of occupational superannuation, and to increase the amount of contributions to a level adequate to fund a reasonable retirement benefit (nine per cent of salary). It proposes

to do this by **compelling** employers – via the taxation powers in placitum 51(ii) of the Constitution – to make contributions on behalf of their employees at the prescribed rates.

The issue of compulsion has caused a philosophical split between the members of the Committee. The Opposition states that it is philosophically opposed to the notion of compulsory savings. The Democrats do not share this view.

In his evidence to the Committee, the Secretary to the Treasury, Mr Tony Cole, showed that there is a clear market failure in Australia in the self-provision of retirement incomes. If desired outcomes – that is, higher standards of living in retirement – are to be achieved, the market failure must be addressed by Government intervention.

The first objective of the SGL – to widen the coverage of occupational superannuation – is supported by the Democrats.

Since 1983 there has been a massive increase in the proportion of the workforce who are members of superannuation funds. The Australian Bureau of Statistics has reported that 72 per cent of the total workforce (aged 15-74) were members of superannuation funds as at November 1991. Some 78 per cent of employees, 52 per cent of employers and 37 per cent of self-employed persons were covered.

This represents a doubling of coverage over the last decade and is largely due to the introduction of compulsory award superannuation.

Although there has been a dramatic increase in employee coverage there is still a significant problem of non-compliance with some award conditions. This is despite the fact that the industrial relations legislation has been amended to assist compliance. As such, it is reasonable to use the greater resources of the Australian Taxation Office to assist in protecting the legal rights of employees. What is important is an equitable outcome, not the particular legislative method which achieves the outcome.

The second objective of the SGL legislation is to provide an adequate level of retirement benefits. The SGL legislation proposes that by 1 July 2000 all employees will have contributions to the value of nine per cent of their earnings made on their behalf by their employers. However, in evidence presented to the Committee, officials from the Treasury indicated that the Government's interim retirement incomes target by the year 2000 is in fact 12 per cent, not the nine per cent specified in the legislation.

This 12 per cent target was first stated publicly in a speech given by the Member for Blaxland, the Hon P J Keating MP, prior to the formal announcement of the SGL in the 1991/92 Budget. The Budget papers stated:

> Consideration will be given to ways, using employee contributions and tax cuts, of increasing the minimum level of superannuation support to 12 per cent by the year 2000.[1]

[1]. 1991/92 Budget Paper No 1, p 4.7.

Evidence before the Committee on the level of superannuation contributions which are necessary to provide adequate retirement incomes confirmed that 12 per cent is a reasonable target (see particularly Chapter 4 of this report).

Large and Small Employers

The SGL legislation before the Committee proposes a dichotomous contributions system. Employers with a payroll in excess of $500 000 are considered to be large employers and are to pay five per cent from 1 July rising to nine per cent by 1 July 2000, whereas employers with a payroll of $500 000 or lower are considered to be small employers and will be liable to three per cent from 1 July rising to nine per cent by 1 July 2000. This dichotomy was not part of the original Accord agreement, but was announced by the Government in the Budget.

In addition, the original timetable as announced in the Budget is different to that in the legislation. The legislation allows a slower phase-in for small employers than the original announcement. Contributions are limited to three per cent until 1 July 1994.

Consequently, there will be no increase in cost for two years for those small businesses which already pay three per cent to their employees. No employer submission received by the Committee has acknowledged this important fact.

Relative to the Accord proposals, it represents a **concession** to small businesses, not a penalty on larger employers. However, it also introduces a significant discrepancy over the short-term for employees, that is, people's compulsory superannuation entitlements vary according to the size of their employer, not their income or their occupation.

Clearly, any reduction in the difference between the two SGL rates will diminish any competitive distortion which arises from a differential cost structure being imposed on business, and will reduce the discrepancies between employees of small and large businesses.

Employment Effects

Each of the employer representatives appearing before the Committee has argued that the SGL will lead to an increase in costs and that this will therefore have an impact on employment. It was further argued that the general economic conditions are still very poor and that this special circumstance must also be taken into account.

Worst case scenario unemployment figures were produced for the Committee by the Treasury. These have been the subject of political manipulation by some members of the Committee, but are clearly not a reasonable estimation of the likely effects of the SGL.

The ACTU argued that employers always oppose all wage claims of employees and that the current position is simply a manifestation of that trend. Further, the ACTU argued the union movement has specifically stated that increases in the SGL will be 'taken into account' in future wage negotiations.

The employers countered that if increased superannuation contributions are legislated, then there is no compulsion for the increased contributions to be taken into account in future wage outcomes.

Clearly there is merit in both positions.

The SGL legislation arose because of an Accord agreement between the Government and the ACTU. There is no doubt that at the time the Accord was agreed to, the view within the Government was that there would not be a severe recession. Subsequently, the Industrial Relations Commission refused for a variety of reasons to ratify the proposal to increase award superannuation from three per cent to six per cent at one per cent per annum. This independent rejection of the proposal on economic grounds also cannot be ignored.

Recommendations:

As noted above, the Government has already altered the implementation timetable without altering the final target level of contributions. Given the concerns about the possible short-term employment consequences of the levy, the implementation schedule should be altered to reduce the proposed five per cent levy on large employers from 1 July 1992 to four per cent.

In addition, the Democrats consider that raising the threshold from $500 000 to $1 million will mitigate as far as possible any adverse employment effects in the short-term.

Furthermore, the Democrats insist that the ***Industrial Relations Act 1988*** *be amended to make clear that the employers' liability under the SGL must specifically be taken into account by the Australian Industrial Relations Commission when making wage decisions.*

Equity Problems of the SGL Proposals

The legislation before the Committee proposes that all employees who earn between $3 000 and $80 000 be recipients of the same percentage of income in the form of superannuation contributions. ACOSS and other groups have argued that very low income earners may be worse off if these proposals are implemented.

Certainly for people earning less than the income tax threshold ($5 400) there will be a disadvantage if future wage increases are taken as superannuation contributions. This disadvantage arises because superannuation contributions and the fund earnings are taxed at a rate of 15 per cent. If the money was paid as wages no tax would arise.

The unions and the Government argue that the option of automatic wage rises to very low income earners is not a realistic option because of the fragmented Federal/State industrial relations tribunals and the lack of industrial muscle for this section of the workforce.

In addition, the charges for administration and life insurance premiums are normally levied on a flat basis and hence impact much more heavily on low income members of superannuation funds.

These problems are not insurmountable. There could be an exemption to the contributions tax in respect of low income earners. A low income earner could be defined as somebody who earns less than a specified amount, say $6 000. This would increase the complexity of the system, yet it would improve the equity. Such trade-offs are common and desirable in taxation systems.

The administration and other charges should be limited to a certain percentage, say five per cent, of a fund member's accumulated benefit or contributions. I favour a limit with respect to contributions because this exempts people who cease employment and hence cease contributions. This eliminates the problem for casual or itinerant workers who have small superannuation benefits eaten up by charges because they have not made any contributions for long periods of time.

If such exemptions and charge limitation measures were introduced, there does not appear to be an equity problem in commencing the SGL at $250 per month. The increase to nine per cent will significantly diminish the relative size of this problem.

Recommendation:

It is recommended that the law governing trustees be amended to make clear that different rates of administration charges may apply to members of superannuation funds, and that all such charges be limited to five per cent of the contributions of low-income earners.

The Democrats are extremely disappointed that despite repeated negotiations on this point, the Government has refused to agree to such a proposal.

Wage Settlements

The equity problems referred to above can be more than offset by a situation where the national wage increase negotiated by unions on behalf of all employees is paid as a flat rate amount as opposed as a percentge increase.The Democrats support this kind of arrangement and feel very disappointed that the advantages of this type of arrangement has been ignored by advocates of the position of low income workers.

Recommendation

The Democrats recommend that the Government support flat rate wage settlements in submissions to future national wage cases and in negotiating future wage Accord agreements with the ACTU.

Future supplements to Superannuation

One further issue which has the potential to radically benefit low income earners is the distribution of the additional three per cent referred to in page 2 of this chapter.That is, apart from the nine per cent in the SGL legislation, the Govt apparently has an intention to direct an income tax cut into the superannuation accounts of individual taxpayers.

It is this amount which is without doubt the most crucial when assistance to the lower paid is concerned.When this amount is distributed, it is essential that it be distributed on an equal per capita basis.That is, every member of a superannuation fund should obtain the same amount of the tax cuts. Such an outcome would benefit low income earners and would massively benefit very low income earners.Indeed in an extreme case this flat rate amount could be larger than the nine per cent of their income otherwise payable under the SGL.

Recommendation

That the Government distribute the 'additional three per cent' which is contained in the Government's interim retirement income target of 12 per cent by way of a flat rate income tax cut distributed to all members of superannuation funds so as to further increase the retirement income of low income earners.

One further matter must be mentioned in any discussion on the equity of the legislation before the Committee. The major equity problem in the superannuation system concerns the distributional impact of the $3.5 billion taxation expenditure.

This matter is not dealt with in this legislation, although it will be considered by the Senate later in the year. The view that the rejection of the SGL legislation would in any way address the inequities inherent in this system is completely incorrect.

Flat Rate Superannuation Arrangements

The SGL raises a further question of equity.

The reliance on identical percentage-based SGL liabilities across the income range of $3 000 to $80 000 clearly confers massive benefits on higher income earners relative to lower paid employees. This is somewhat mitigated by the fact that many highly paid employees already enjoy substantial superannuation benefits and so may not gain anything from the legislation.

Apart from the limitation on charges as recommended above, one measure which would increase the equity of the SGL is to encourage the provision of flat rate superannuation arrangements whereby all employees obtain the same amount of superannuation benefit from their employers irrespective of their individual income. Such arrangements already exist in some industries and have been successful.

It is proposed that an additional category of superannuation arrangements should be recognised and encouraged by the SGL legislation. This would involve allowing an employer to extinguish his or her liability to employees by way of a qualifying enterprise or industry superannuation arrangement. This could be through either an industrial award or some other type of employment contract.

Under such an arrangement, an employer would be able to satisfy his or her SGL requirements by providing **aggregate** superannuation contributions equal to those which are required under the legislation, even though not all employees are receiving the required amounts.

Such an arrangement provides flexibility in allocating superannuation benefits. It would ensure that employers cannot reduce the total amount of SGL liability, although they can provide additional benefits to lower income earners. Employers are then free to top up any individual's superannuation benefits as a normal part of salary negotiations.

The ACTU has given evidence to this Committee that it does favour flat rate superannuation arrangements in certain circumstances. Such arrangements can only increase the equity of the superannuation system. They would have to be negotiated between employers and employees, just like all other industrial conditions.

The final benefits provided would not be determined by the salary of an individual employee but would satisfy a community standard on what constitutes a basic retirement income – this is basically what the age pension system achieves.

The Committee heard evidence from the NSW Coal Association that it has successfully managed a flat rate superannuation scheme for many years. The arrangements enjoy wide support amongst the employees of the industry, especially the lower paid workers.

Recommendation

That the Bills be amended to allow employers to satisfy their SGL liabilities by making contributions to a 'qualifying enterprise or industry superannuation arrangement' which provides equal payments to all employees irrespective of their particular income. Part-time and casual workers would receive a proportionate payment according to hours worked.

Technical Problems

There is considerable doubt about the technical structure of the legislation.

To avoid having to pay the SGL, an employer has to make a contribution at the prescribed rates to a **complying superannuation fund**. This is a defined term in income tax legislation. A complying fund is one which qualifies for concessional taxation treatment – that is, is taxed at 15 per cent – and which also adheres to all the other regulations concerning disclosure, trustee representation, et cetera as specified in the *Occupational Superannuation Standards Act* and associated Regulations.

Unfortunately, a fund is not a complying fund unless a certificate of compliance is issued by the Insurance and Superannuation Commissioner after the end of the financial year. As such, employers cannot be certain of technically complying with the legislation even where they have made the appropriate superannuation contributions.

Recommendation

A technical amendment is necessary to deem that a fund which was a complying fund in the previous year continues to be a complying fund unless the employer had reasonable grounds to believe that the fund would not be a complying fund for the year in question.

Another technical matter is the question of the definition of employee. Subclause 12(10) of the Administration Bill includes a local Government councillor as an employee. This issue first arose when the Taxation Commissioner ruled that a councillor was an employee under the *Income Tax Assessment Act 1936* and hence liable to PAYE tax deductions. This was overturned by a court decision and the Government subsequently announced its intention to legislate to include local councillors in the definition of employee. This decision was subsequently reversed.

It is considered reasonable to treat full-time councillors who receive large remuneration in the same manner as State and Federal members of Parliament. However, because of the special nature of councillor remuneration – that is, incidental expense reimbursement – it is not appropriate to deem all councillors to be employees.

Recommendation

That the definition of 'employee' be amended to exclude local government councillors except for those earning full-time salaries in respect of their duties.

Another technical problem is that of the time and steps necessary to amend trust deeds so as to ensure that funds meet the prospective standards necessary to qualify as a complying superannuation fund. The Government correctly argues that there is over a year for the necessary legal work to be done before any SGL liability arises in respect of an employee. However, the position for employers in respect of employees who cease employment after 1 July 1992 but before trust deeds are satisfactorily amended is unfair. Employers will not be able to make qualifying contributions to the relevant fund. As such, an employer will incur a non-tax deductible SGL liability for something which is beyond his or her control.

Recommendation

That a transitional provision be enacted to permit tax deductibility for SGL payments made in respect of 1992-93 on behalf of employees who terminate employment during that period.

One other anomaly in the legislation concerns the situation where an employee refuses to join a superannuation fund. In such a situation, rare as it is, an employer would incur a non-deductible SGL charge even though he or she was not responsible for the non-provision of superannuation contributions.

If the employee had joined the fund, the employer's contributions would have been tax-deductible. Clearly, this situation is unfair.

Recommendation

That SGL payments made by employers in respect of employees who refuse to join a superannuation fund be tax-deductible.

General Reform of the Superannuation System

The legislation before the Committee does not address the fundamental design of the retirement incomes system. Indeed, from the evidence given by Treasury officials, the legislation before the Committee does not even seek to fully implement the Government's interim retirement incomes target of 12 per cent by the year 2000.[2]

The Government's position is that this legislation simply attempts to create a much larger pool of retirement savings, and that the fundamental design of the retirement incomes framework is a separate and distinct issue which must be dealt with in isolation. In other words, the Government is saying 'pass this legislation and trust us to deal with the other outstanding issues'.

The Australian Democrats do not agree with this approach. As such, the Government has provided a written assurance that it will legislate during the Budget session in respect of the vital area of prudential supervision of superannuation funds.

Furthermore, the questions of fair and responsible taxation arrangements and the transition to a more realistic preservation age have also been agreed to in principle by the Government.

The areas which continue to need reform include:

2 SG evidence, p 10.

- the prudential regulation (that is, the financial supervision) of superannuation funds to ensure that members' interests are protected;

- the interaction between the superannuation system and the social security system in such areas as the preservation age, access to age pension fringe benefits for superannuants and the differential taxation regimes which apply to age pensioners and self-funded retirees;

- the current income tax concessions which are highly regressive and strongly favour high income earners;

- the appalling lack of regulation, and disclosure, of the fees and charges which superannuation funds may impose;

- the complexity and incomprehensibility of the superannuation system to most ordinary people;

- the appropriate treatment of accrued superannuation benefits on the breakdown of a marriage;

- the lack of access to superannuation for those not in the workforce;

- the complete lack of regulation of the investment practices of fund managers and the ignoring of the long term economic needs of Australian industry, particularly with respect to development capital; and

- the lack of a credible independent low cost non-legalistic disputes resolution mechanism which will protect the rights of fund members.