

Portfolio

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CHEMIST'S BITTER PILL

A pharmacist with a turnover of between \$500,000 and \$1 million a year did not lodge income tax returns from 1984 to 2002, according to a recent report by the Australian Taxation Office's cash economy taskforce. He was detected when registering with the ATO for an Australian business number (ABN) and claiming GST refunds.

The non-complying pharmacist is one of several case studies included in the taskforce's report and highlighted in the *Weekly Tax Bulletin*, published by ATP. Other examples include:

■ An individual who did not lodge an income tax return for 30 years and a BAS for three years. A tax agent quoted in the taskforce's report said the crackdown of the ATO had prompted him to seek tax advice about his failure to comply.

■ A partner in a cafe with an estimated annual turnover of \$120,000 operated the business without ABN or GST registration. The other partner was found not to have lodged an income tax return since 1985.

MICHAEL LAURENCE

Super's ho-hum tax cut

Trimming the contributions surcharge might help retirees afford an extra sandwich and milkshake but little else. By Michael Laurence

The marginal cutting of the super contributions surcharge for higher-income earners under legislation passed late last month will lead to only a minuscule increase in retirement savings for baby boomers intending to finish working in the next decade. Even those with large annual contributions will save relatively little extra over the short to medium term from the gradual cutting of the top surcharge rate from 15% to 12.5% over the next three years.

Research by the Association of Superannuation Funds of Australia (ASFA) shows that average annual contributions for those caught by the full surcharge is \$25,000 a year. The surcharge cut will save higher-income earners in this category just \$125 in tax this financial year; \$375 in 2004-05; and \$625 in 2005-06 and subsequent years.

ASFA calculates that it would take 30 years for a person earning \$125,000 a year with \$25,000 in annual contributions to increase retirement savings by \$31,000, allowing for the compounding effect, because of the surcharge reduction. In reality, this means that relatively few members of today's workforce will enjoy large increases in their retirement savings from the surcharge cut. The rare exceptions will include those who earn a very high income within 10 years of joining the workforce and have many years left before retirement.

Superannuation researcher Alex Dunnin is dismissive of the surcharge cut. Dunnin, the research director for Rainmaker Information, describes the surcharge reduction as being "so small it is almost meaningless" for most high-income earners. He points out that the super fund members subject to the full surcharge had been paying a total of 30% tax on super contributions (the standard 15% super contributions tax plus the maximum contributions surcharge). "The cutting of the tax on contributions to 27.5% by reducing the surcharge is hardly going to encourage someone to contribute to super."

Dunnin says the small effect of the surcharge reduction emphasises the need for fund members to concentrate on finding super funds with reasonable fees and solid returns. Where appropriate, fund members should consider funds with investment choices that allow members to maximise their returns. "The real game in town is getting your investment returns to work for you. Tinkering with contributions taxes, as this legislation does, is a sideshow." He suspects that superannuation taxes are not going to be cut in any worthwhile way in the future. "Where is the political payoff for a government?" He says

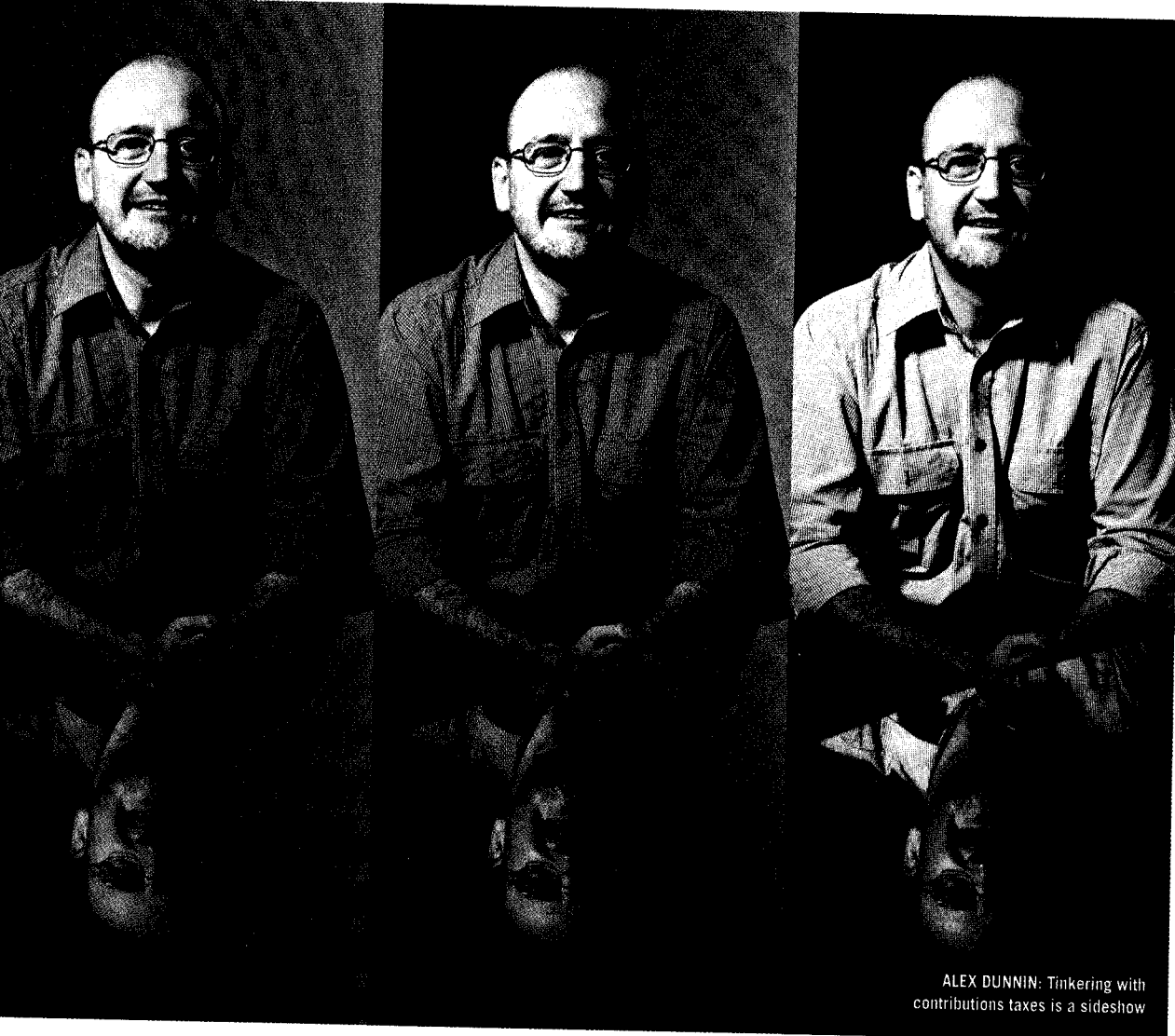
an overall income tax cut would be a much more effective way for a government to win votes.

The surcharge generally begins to apply for those with so-called adjusted taxable incomes exceeding \$94,691 (the threshold amount for 2003-04) and increases progressively to the maximum surcharge rate for those earning \$114,981 and above. (The actual surcharge rate for those subject to the impost at below the top rate is calculated using a complicated formula based on the full rate. The ATO has not yet updated this formula to reflect the surcharge cut.) Adjusted taxable incomes for the purposes of the surcharge include salaries, the value of fringe benefits subject to the fringe benefits tax, investment income and capital gains, compulsory employer contributions, salary-packaged super contributions and any other super contribution for which a tax deduction was claimed. The new top surcharge rates are 14.5% for 2003-04, 13.5% for 2004-05, and 12.5% from 2005-06.

In measuring the immediate and long-term effect of the reduction in the surcharge, Dunnin's approach differs from ASFA's in that he analyses the example of an executive earning \$120,000 a year with only the compulsory employer contributions of 9% a year. (For the sake of the exercise, Dunnin assumes the executive pays contribution charges of 1% and the fund earns 8% a year.) He calculates that the executive will increase retirement savings by \$4800 over 10 years because of the surcharge reduction, once the investment returns are taken into account. "This is less than \$500 a year." Dunnin says this reduction in the surcharge, although "helpful", is equivalent to a very modest reduction in annual investment fees charged by a fund.

The Howard Government's introduction of the surcharge in the federal budget of August 1996 is perhaps its most-criticised action within the superannuation industry. Apart from the detrimental effect on retirement savings, the industry was incensed because the administrative difficulties of collecting the impost was handed to the super funds. Dunnin believes that the Government did not fully realise that superannuation was already so highly taxed and inadequate for Australian's rapidly ageing population.

The chief executive of ASFA, Philippa Smith, recalls what she says was the reasoning behind the introduction of the surcharge: "The Government was facing current budget difficulties and the surcharge was a handy way of getting a revenue stream. There was a shortfall of revenue, and the surcharge was a tax grab."



ALEX DUNNIN: Tinkering with contributions taxes is a sideshow

MICHELLE MOSSOP

CHANGE WILL BE SLIGHT

1 Most high-income earners should not expect a big increase in retirement savings from the slight reduction of the super contributions surcharge from 15% to 12.5% over the next three years.

2 Among the few big winners from the surcharge cut will be fund members with relatively high incomes for their ages and many years before retirement.

3 Apart from increasing super contributions, a smart way to boost retirement savings is to find super funds with good performance and competitive fees.

4 The Howard Government's introduction of the surcharge in the August 1996 budget is widely seen within the super industry as a quick grab for taxes and is one of its most criticised measures regarding super. The tax take for 2002-03 alone is \$1.27 billion.

Murray Wyatt, a director of Morrows Superannuation Consultants, says: "The introduction of the surcharge put doubt in people's minds about whether they should contribute to superannuation." Wyatt adds: "Most people, including high-income earners, are chronically underfunded for their retirements."

Wyatt agrees with Smith about the Government's reasoning behind the introduction of the surcharge, also saying that super was looked upon as a means for a quick tax grab. The surcharge has been a highly effective means of gathering extra tax. From the 1997-98 financial year, the surcharge has earned the Government more than \$3.98 billion in revenue. In 2002-03 alone, the take is \$1.27 billion.

A research paper written by Ross Clare, the principal researcher at the ASFA research centre, points out that the Government had initially expected the surcharge to raise \$450-500 million each year from about 35,000 fund members. Clare writes: "Evidence from Australian Taxation Office officers to the Senate suggests that currently about 900,000 surcharge assessments are being issued a year." (Some taxpayers who are members of more than one fund receive multiple surcharge assessments.)

During the 2001 federal election campaign, the Howard Government pledged to reduce the top surcharge

rate to 10.5% if returned to office, but subsequently could not get the cut passed into law. Labor objected to cutting the surcharge at all, stating that any reduction should be in the standard 15% contributions tax. The Australian Democrats negotiated a compromise deal that involved the progressive cutting of the maximum surcharge to 12.5% if the Government agreed to increase the eligibility for a measure involving the matching of the personal super contributions of low-income earners by up to \$1000 a year. Both measures took effect from July this year after being passed together by Parliament.

ASFA has long been campaigning hard for a reduction in super taxes. Smith says: "We would like to see the surcharge go altogether but [the reduction] is a step in the right direction. Our ultimate mission is to get rid of all front-end taxes [on superannuation], the standard 15% contributions tax and the surcharge. Any step in the right direction needs to be applauded. Something is better than nothing."

Smith says that any reduction in taxes on contributions is lessening one of the psychological barriers to saving in super. She says the expected future budget surpluses should give the Government the capacity to further reduce superannuation taxes. She says co-contributions have "a significant potential to boost retirement savings for people on lower incomes". ●