

SUPER

Yawning indifference

Reducing the superannuation surcharge will have less impact than you might think, reports **John Collett**:

The superannuation surcharge looks set to be reduced from 15 per cent to 12.5 over the next three years, but high-income earners and their advisers are hardly jumping for joy. The research director with Rainmaker Information, Alex Dunning, says for someone earning \$100,000 a year with \$50,000 in superannuation, over 10 years the new surcharge rate will increase their benefit by just \$2386 (see table below). And that is assuming that the 10 years begins after the three-year phase-in period.

"It is a tiny change that will really make no difference," says Anna Carrabs, a director of chartered accountants William Buck.

The change will not encourage high-income earners to put more away in superannuation in "any way, shape or form" says Melbourne planner Kevin Bailey, of The Money Managers.

The controversial surcharge is paid by those earning more than \$94,691 and kicks in at its full 15 per cent on contributions to superannuation once income reaches more than \$114,981. Under the proposed changes before the Senate, the first reduction in the surcharge will be 0.5 per cent this financial year, followed by a further 1 per cent drop for the next two financial years.

Those under the surcharge income threshold already pay 15 per cent in contributions tax. So, the reduction means that in three year's time the high income earners will pay 27.5 per cent contributions tax instead of 30 per cent.

The Government originally proposed that the surcharge be reduced to 10.5 per cent, but in negotiations with the Australian Democrats, which holds the balance of power in the Senate, the Government agreed to 12.5 per cent. The tax retained by not cutting the surcharge to 10.5 per cent will be used to help pay for the super co-contribution scheme, where those earning up to \$27,000 who make a voluntary contribution will have it matched dollar-for-dollar by the Government up to

\$1000 a year. For those incomes of more than \$27,000 the "cap" of \$1000 reduces gradually, phasing out at an income of \$40,000.

The Association of Superannuation Funds of Australia (ASFA), which has been lobbying hard for both changes, says that even taking into account the reduced tax take because of the surcharge reduction, the Government will still raise \$1 billion in annual revenue by 2007-08.

"The front end taxed on superannuation can be unfair, inequitable, and erode the efforts of people trying to do the right thing and save for their retirement," says ASFA.

However, Carrabs says superannuation, even with the tax on contributions of 30 per cent, was always a tax-effective investment for older high earners, compared to their marginal tax rate of 48.5 per cent.

Carrabs says, however, that for those in their late 30s, such as herself, superannuation was only just starting to "come into focus". Many of her high-income clients, she says, prefer to borrow to invest, something they cannot do inside super.

A financial planning specialist for HLB Mann Judd, Michael Hutton, says he often recommends that clients on high incomes in their late 40s start making large voluntary contributions to superannuation, but agrees that the reduction is not going to see an increase in voluntary contributions by the younger high-income earners.

Dunning says the "real" costs of superannuation for high earners, especially as they are likely to have or will have big account balances, are the ongoing fees.

Dunning says the fees paid inside superannuation, which are usually levied as a percentage of the account balance, will have a much bigger impact on the size of the eventual benefit than small reductions in the contributions tax.

Professor Ian Ramsay, director of the Centre for Corporate Law and Securities



Big deal: Reduction of the super surcharge has left some underwhelmed. Photo: Getty Images

Regulation at the University of Melbourne, noted in his report for the Australian Securities and Investments Commission, released last year, that for each 1 per cent of annual fees, over 20 years the final benefit is reduced by 18 per cent.

Carrabs says many high-income earners choose to run their own superannuation fund because they like the flexibility of being able to include a wider range of investments in their fund and avoid fund managers and their fees.

They find that the money saved in fund manager and fund administrator fees will far outweigh the compliance and other costs of establishing and maintaining a self-managed superannuation fund.

With the past three years being the most poorly performing for investment markets since the introduction of compulsory superannuation in the early 1980s, the focus has been on fees and taxes. But the single biggest determinant of the size of the retirement nest egg are the investment returns of the superannuation funds.

Dunning says that just earning 1 per cent

points more each year, after fees and taxes, through choosing better investment options or being in a smarter fund, would more than make up for any reduction in fees and taxes.

"So while contribution fees and taxes are something we obviously don't want to pay if we can avoid them, the stark reality is the rolling annual performance is where the action really is," says Dunning.

He says blaming contribution taxes and fees for poorly performing superannuation is a "side show". Seeking out better performing superannuation funds sounds fine in theory, but most employees have no control over which fund their employers' superannuation guarantee goes to. They are stuck with underperforming funds.

It looks as though the Government's push for portability of superannuation, which is before the Senate and is a sort of first step to full choice, will fail. Under the proposal, after changing employers the employee would be allowed to direct the superannuation contribution to the superannuation fund of their choice.

TAX CUT: SMALL GAIN OVER 10 YEARS

SURCHARGE	TOTAL CONTRIBUTIONS TAX	BALANCE
15%	30%	\$171,696
12.5%	27.5%	\$174,082
10.5%	25.5%	\$176,123

ASSUMES SALARY OF 100,000 A YEAR, TEN YEARS OF SUPERANNUATION GUARANTEE CONTRIBUTION STARTING ON JULY 1, 2006 AFTER 3-YEAR PHASE-IN OF REDUCTION COMPLETE

SOURCE: RAINMAKER INFORMATION