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FIVE REASONS LABOR'S SUPERANNUATION CHANGES WOULD DAMAGE AUSTRALIA

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In a speech to the Chifley Institute last week, Opposition Leader Bill Shorten announced that the Labor Party would introduce further changes to Australia's compulsory superannuation system.[1] The key change is to abolish cash refunds for so-called excess dividend imputation credits. This means any superannuant whose tax liability is negative following the franking of dividend payments from companies would no longer receive a tax refund – resulting in a higher effective tax rate.

Dividend payments are fully refundable to avoid the double taxation of company profits. Companies initially pay 30 per cent tax on their profits. A share of this post-tax profit can be paid out as a dividend to shareholders. If shareholders pay tax on this post-tax dividend, then that income will have been taxed twice: first through the company tax, and then through income tax.

The Changes Could Affect 15 Million Australians

The Australian tax system allows for the full franking of dividend payments payed out by Australian companies to Australian shareholders. This means the tax which shareholders pay on dividends is the difference between their marginal income tax rate and the company tax rate of 30 per cent. If a shareholder is taxed at a rate lower than 30 per cent then they receive a tax refund. This refund equals the percentage point difference between their marginal tax rate and the company tax rate, multiplied by the outstanding dividend amount.

Initial analyses suggested that around 1.1 million Australians would be directly affected by the proposed changes. And that more than 610,000 Australians on the lowest annual incomes could lose an average of $1200 a year in tax refunds.[2] Over 10 years, on Labor's own policy calculations, the proposed changes would confiscate a further $59 billion in higher taxes from Australians. This is in addition to the record $540 billion Commonwealth, state, and local governments will confiscate from Australians through taxes this year.

However, it will not just be current retirees who will be affected. All 15 million prospective retirees who hold a superannuation account stand to be affected. This is because the changes would alter the relative benefits of investing in Australian companies which pay relatively high dividends compared with non-Australian companies and Australian companies which pay relatively low dividends. Whether this is good economically is mute. It will cause all 15 million prospective superannuants, or those who manage their funds, to re-assess their investment strategies.

The Changes Will Hike Taxes; Not Reduce Welfare

Bill Shorten described the current fully refundability of dividend credits as a form of "millionaire welfare".[3] This is false. Those who receive a tax refund are doing so because they have paid tax which is in excess of their legal liability. This is no different to those millions of Australian who receive a tax refund on the income tax they have paid – they have been taxed in excess of their legal obligation and, rightly, receive a compensatory refund.

The reason so many Australians receive a tax return on their superannuation earnings is because superannuation earnings and withdrawals are typically taxed at a lower rate than labour income. This is to encourage people to save for their own retirement which is an explicit objective of the superannuation system.

The Changes Would Reduce Investment in Australia

The current imputation system creates an incentive for investors to invest in Australian companies. This is because dividend payments can only be refunded to Australian investors who have invested in Australian companies. Reducing the refundability of dividend payments will reduce the expected return of investing in Australian firms. This will increase the cost of capital in Australia as investors will demand higher returns to compensate for the loss of investment income, and hence the volume of investment will decrease.

Business investment is currently just 12 per cent of GDP, which is below the rate which prevailed during the economically-hostile Whitlam years. Low business investment is a key factor which is holding down productivity and wages growth.[4]

The Changes Would be Retrospective

Retrospective legislation is legislation which applies to decisions taken in the past. Current retirees have structured their retirement investment income over a period of decade's according to the rules that prevailed at that time. Those decisions, taken in the past, will be affected Labor's proposed changes. Current retirees cannot revisit the past and alter their investment decisions to accommodate Labor's proposed changes.

Retrospective legislation is widely regarded as a transgression of the rule of law because it is arbitrary and inconsistent with reasonable expectations of the affected parties.

The Changes Would Add Further Uncertainty to Superannuation

Saving for retirement through superannuation or other means is necessarily a long-term strategy. For people to have confidence in their investment strategy, the rules which surround that investment must be clear and stable. However, repeated policy changes to the superannuation system, by both the Coalition and Labor parties, have eroded the trust and certainty that Australian's have in the superannuation system.

Armed with the knowledge that investment in superannuation is no longer protected from retrospective tax hikes from either party, Australians will invest less in the superannuation system. This is likely to make them more dependent on a public pension, either in part or full. This, in turn, erodes the efficacy of superannuation as a vehicle for Australians to be self-sufficient in retirement.

What is more of a concern, though, is that Australians do not have a choice to not invest in superannuation. A portion of their wages are forcefully placed into superannuation accounts. Australians are therefore unable to opt-out of the system if they believe it is no longer operating in their best interest. They are therefore unable to avoid the tax hikes imposed by both parties unable to fix the Budget through reduced expenditure.

1 Benson, Simon; Brown, Greg; and Kelly, Joe, "Shorten's class-war $59bn tax on wealthy shareholders, retirees, superfunds", *The Australian*, (13 March 2018)

2 Benson, Simon and Kelly, Joe, "Bill Shorten's tax grab to affect the lowest incomes", *The Australian*, (14 March, 2018)

3 Livingston, Angus and Jennings, Jennifer, "Time to end 'millionaire welfare': Shorten", *The Courier*, (14 March 2018)

4 Wild, Daniel, "Business Investment Lower than Whitlam", Institute of Public Affairs, Melbourne, Victoria, (2017)

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