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The General Manager *✓ m 10/8*
Superannuation, Retirement & Savings Division
The Treasury
Langton Crescent
PARKES, ACT 2600

Dear Sir or Madam

**Re: Changes to self managed superannuation funds & pensions in May 2004
Budget**

I would like to make the following submission to you in relation to your inquiry into the proposed changes to defined benefit provisions of the superannuation legislation.

My wife and I are in our late 50's and are members of a self-managed superannuation fund (SMSF) with which we hope to fund our retirement. Through a program of diligent contributions and prudent investments, the value of our fund now exceeds our lump sum RBL. This was not of great concern to us because the trust deed of our superannuation fund specified the possible use of defined benefit pensions (ie including a lifetime complying pension for 50% or more of our superannuation benefits), a strategy that effectively doubles the amount of money we can receive as a rebateable pension in retirement, before normal taxation is applied to the pension. I suspect that the thinking behind this was to encourage the use of annuities, rather than the removal of lump sums which can be frittered away easily, leaving the retiree no option other than to apply for a Government old-age pension. Not everyone can take advantage of this opportunity but it does reward those people who have saved diligently and invested prudently when building up their superannuation.

My wife and I have been pursuing this strategy for many years. However, we had not planned to retire before 30 June next year. Therefore, the effect of the changes to SMSFs in the May 2004 budget is to make it impossible for our SMSF to pay a lifetime complying pension other than by contracting with a third party to provide the pension. The disadvantages in doing this are:

1. all third parties charge fees for their services
2. on the member's death, any SMSF assets in the third party's control (shares, cash, property) become the property of the third party

This contrasts with the situation that applies when the SMSF manages the lifetime complying pension where the trustees of the SMSF are not paid for their services, and any assets remaining after the member's death may be inherited by the member's beneficiaries.

In my own case, I see no point in employing a third party to manage a lifetime complying pension. I don't believe that their investment decisions are likely to be in any way superior to my own. For example, AMP's recent history gives me no confidence in their ability to look after my affairs. Why should I be forced into the arms of such a third party and at the same time forsake any rights to pass on the remains of my superannuation savings to my children?

I have also looked at the market-linked pensions which the government has suggested are adequate substitutes for the lifetime complying pension. They are clearly inferior because:

1. they are payable for a fixed term rather than for life. (I understand from comments by a number of actuaries that the probability of my wife and I outliving the term of the pension is about 40%);
2. the rate of the pension may bear no relation to our living expenses; and
3. a significant part of the pension may be non-rebateable because the pension is valued by reference to the account balance rather than the rate of the pension.

So it may be that having planned our retirement on the basis of the rules pertaining prior to the budget, we find that the system has misled us into making excess contributions. These contributions will have attracted 15% tax and the 15% surcharge on contribution, and will be taxed at 48.5% when they are paid to us as a pension. So they will end up being taxed at 78.5 cents in the dollar when they are finally paid out as a pension. This rapacious level of taxation is absolutely outrageous! It gives no encouragement to anyone who strives to make provision for retirement. It also illustrates the hollowness of claims in the Australian Financial Review by the Australian Taxation Office alleging that superannuation is being used to rot the tax system. Who, one might ask, is rotting whom?

Moreover, if one is successful in investing the superannuation funds such that significant capital gains are made from an asset held longer than 12 months, these are initially taxed at 10%, but will attract a further 48.5% taxation on payout in the form of a pension whereas the same capital gain made outside the superannuation fund attracts 25% tax.

What should be done about this totally unacceptable situation? I suggest the following alternatives:

1. Accrued benefits as at May 2004 and earnings arising from them should be able to be paid as lifetime pension. To do otherwise is to produce a situation in which the Federal Government has allowed contributions to superannuation funds to be made under false premises. The situation may be likened to an IPO in which investors are allowed to purchase shares and the Prospectus is subsequently found to have been false or misleading.
2. Allow any contributions in excess of the RBL to be withdrawn from the SMSF on payment of an appropriate level of tax i.e. 18.5 cents in the dollar for any contributions which have already attracted 15% tax and 15% levy, 33.5 cents in the dollar on any earnings on these contributions which have already been taxed at

15%, and 15 cents in the dollar on any capital gains which has already been taxed at 10%. Withdrawals would be permitted until the fund begins paying a pension.

3. Require the excess funds to remain in the SMSF but apply the reduced taxation rates in 2 on payout as a pension.
4. Allow the excess funds to be converted to undeducted contributions at any time by paying the reduced taxation rates in 2.
5. A combination of 1 – 4.

I personally favour option 5. It allows members of SMSFs greatest flexibility in preparing for retirement and ensures that they never pay more than 48.5 cents in the dollar on income and 25 cents in the dollar on capital gains held longer than 12 months.

I hope you can understand the resentment felt by members of SMSFs who find their retirement plans disrupted by poorly thought out measures such as those proposed in the 2004 budget. What confidence can one have in a system that keeps on changing in a manner that is obviously detrimental to the very people it hopes to attract? Why should anyone bother to try and make provision for retirement when such obstacles are placed in one's path? Why not just dispose of assets and apply for a government pension when the money runs out?

I hope you will take this information into account in deciding how to respond to your brief in relation to your inquiry into superannuation.

Yours faithfully



Ben Korman