

## Purpose

The purpose of this paper is to seek a review of the taxation treatment applied to interest and earnings on superannuation.

## Background

To date the Superannuation Industry has been - fortunate in the reform of taxation on superannuation. The tax system on the recommendation from the taskforce and the ASFPNG have seen taxation on superannuation overhauled. We have been fortunate that Treasury has been - receptive -to our proposals. In the 2003 Budget the following reforms were implemented

Tax is levied on your superannuation at the time that you withdraw. The tax system is designed to favour long-term contributors and substantial tax benefits are incurred for those who remain in the system long term. Different rules therefore apply depending on the years of service for employer and interest components of superannuation.				
Years of Membership	<5 years	<5 years and <9 years	<9 years <15 years	<15 years
Rate of Tax	Marginal Rate of Tax	The lesser of 15% or the marginal tax rate	The lesser of 8% or the marginal tax rate	2% tax on interest and employer contribution
A concessional rate of tax of 2% also applies to distributions where the payments relate to benefits accrued before 01 January, 1993.				

Similarly, tax on earnings was reduced below the company tax rate of 30% to 25% (the rate prevailing before the increase in the company rate).

The tax application on superannuation in PNG is far less complicated and more user friendly than in Australia, and we need to keep it that way. We are indeed fortunate that Superannuation in PNG does not carry excessive legislative baggage.

## Proposed Further Reform of Taxation on Superannuation

Nasfund believes that - there is still one anomaly that requires addressing.

Currently tax is applied on superannuation earnings at 25% on income generated from fixed interest securities of less than 5 years maturity- which is unavoidably the predominant form of investment in present circumstances for most Funds. ---Earnings are then taxed again at the member level on member withdrawal. This appears to be unfair. –

- a Member currently on the maximum tax threshold could pay through the Fund 25% on the income generated and then if withdrew under five years of membership, pay a further 47%. In effect the taxation would be 72% over all on the income.
- A more common example would be a member with between 5 and less than 10 years standing, who has to pay 15% on exit- a total tax rate of 40% on earnings

These are penal rates on mandatory contributions.

Moreover, with the recovery in confidence in superannuation, there is growing interest among some members in voluntary contributions, which would be to the benefit of the country as well as the member, but the double taxation of fund earnings constitutes a barrier to this development.

The situation is actually much worse than it appears when it is remembered that taxation applies to nominal, not real, earnings.

- for example, if the rate of interest on the fixed interest earnings of a Fund is, say, 10%, and the rate of inflation is 7.5%, then the real return is only 2.5%- and after tax at 25%, the real return on members' funds is zero.
- but the member on exit is still required to pay tax on the after-tax nominal earnings, meaning that he has suffered an outright loss in real terms on his savings.

Nasfund believes that this is iniquitous and that tax on income on withdrawal should be awarded the same status as member contributions, (i.e tax is paid once at the source only [? Do you mean ‘ in the hands of the fund, & not upon exit’?])

**Recommendation**

That the ASFPNG write to Treasury seeking a review on the taxation treatment on income with the view to amending the Tax Act to remove taxation on interest on withdrawal.

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