Do The Rich Need Super Support?

2 April 2013

Superannuation reform should have been be a no-brainer for Labor. The party looks set to continue John Howard's loyalty to the rich by backing "battlers" on $250,000 a year, writes Ian McAuley.

The present Federal Government has the unfaltering capacity to take a good idea and to handle it so badly that its opponents can present it in the worst possible light.

So it was last week, when the Government ran some ideas about superannuation up the flagpole and not many people saluted. The broad policy issue about how to allocate scarce public revenue was drowned out in a technical argument about costings and in emotive rhetoric, such as the claim in the weekend Financial Review editorial, claiming Labor's policy has "degenerated into class-war politics".

The height of absurdity was Joel Fitzgibbon's statement that "in Sydney's west you can be on a quarter of a million dollars family income a year and you're still struggling". Fitzgibbon talked about coal miners in his electorate earning $100,000 to $140,000 a year who, he considered, were not wealthy.

I don't know what circles Fitzgibbon moves in. When the Bureau of Statistics last surveyed household income in 2009-10, it found only one household in 35 with an income of $250,000 or more and that median household income was around $65,000. Perhaps the "coal miners" to whom he refers are actually investors in coal companies, who seem to be well-represented in the ranks of NSW Labor.

The reality is that superannuation tax concessions are expensive. Treasury estimates that concessional taxation of contributions costs $14.3 billion a year, and will cost $17.4 billion within three years, and that concessional taxation of fund earnings costs $17.1 billion a year, projected to rise to $25.1 billion a year. To put these figures into perspective, Commonwealth expenditure on "income support for seniors" (i.e. the age pension) costs $36.7 billion a year and is projected to rise to $44.7 billion by 2015-16.

In simple terms, Commonwealth expenditure on superannuation is growing 50 per cent faster than expenditure on age pensions, and will cost more than the age pension within four years. Prime Minister Gillard is rightly couching her concerns in terms of the long-term sustainability of the system.

There will inevitably be disputes about the accuracy of cost estimates. Superannuation concessions are costed as "tax expenditures" to use Treasury jargon, which are estimated on the basis of revenue forgone. Treasury does not make the same claims of reliability for these figures as it does for projections of outlays. Quibbles over the precision of these figures, however, are mere distractions — the facts are that these concessions are expensive, and that they're growing rapidly.

The broad policy problem facing this Government, the next Australian government, and indeed all governments in prosperous countries in coming years, is the way demands for income support, not only for the aged but also for the unemployed and those with illness or disability, are crowding out other areas of needed public expenditure (pdf).

A modern economy capable of holding its own in a competitive world needs a range of public goods which the market cannot supply at all, or cannot supply efficiently. These include defence, education, health care, infrastructure and many others. In some of these areas the private sector has a role in their delivery, but the bulk of funding has to come from the public purse — private mechanisms to fund such services, such as private health insurance and road tolls, are much more expensive and inevitably much more inequitable than systems based on public revenue.

At the same time, however, income disparities are widening in most countries — this has been an inevitable consequence of economic liberalisation and opening up to global competition. These processes have generally been beneficial, but many have been left behind in the new waves of prosperity. These developments put demands on welfare budgets, in addition to the demands associated with an ageing population.

So far governments have coped poorly with these conflicting demands. Many European countries simply went on a borrowing binge, trying to maintain both a generous welfare state and public services. That approach has clearly met its limits. The US went on a similar borrowing binge, not to sustain a welfare state, but largely to support a hungry military establishment and to keep taxes low.

In Australia during the Howard administration, the approach was to squeeze public expenditure in areas such as education and infrastructure — the very investments needed for international competitiveness — while sustaining generous welfare payments, particularly what we generally refer to as "middle class" welfare. Superannuation concessions need to be seen in this light.

Boosting middle class welfare can be seen as a clever political strategy in an economy in which, as the Productivity Commission has found, incomes of the employed workforce are widening. There are fewer people in the "middle" than there once were, but because they tend to be swinging voters, they command disproportionate attention from governments.

The Howard measures went further than simply boosting middle-class welfare however, and, as Richard Denniss of the Australia Institute points out, one third of the benefits of superannuation tax concessions go to the most prosperous tenth of the population.

Why the Howard government was so generous is a mystery. A political realist may say it was a parting gift to a class who had been so loyal to the Coalition, but, in this age of political correctness, we're not allowed to talk about "class".

Possibly it was an attempt to boost private saving. In all the hype about the "virtue" of the Howard government budget surplus contrasting with the "profligacy" of the Rudd- Gillard Government (a political presentation that rests on a fundamental misunderstanding of economics), little has been said of the huge accumulation of private debt during the Howard years. Encouraging the well-off to invest in superannuation may have been a quick and easy way to compensate for that trend.

Besides these rational explanations, we should not dismiss sheer policy stupidity. After all, the Treasurer at the time was Peter Costello.

The Howard government's legacies to the present government and to its successors have been an expensive program growing at a rate of 10 per cent a year, and the political problem that even the very well-off have an entrenched sense of entitlement and even a sense of dependence.

There is no doubt that people with low and modest incomes need public support in order to enjoy a dignified life in retirement. That support generally relies heavily on publicly-funded pensions, supplemented with encouragement, compulsion and subsidisation for private saving. The choice of the best mix of these measures is largely a technical question.

But how much support do the well-off require? And how can they be weaned off government dependence? No doubt it is possible to have a struggle to make ends meet on a $250,000 or higher income. We have a tendency to confuse wants with needs, to make our purchases on the basis of what we can afford to spend rather than what we need, and to engage in expensive arms races for positional goods, such as the "best" private school for our children, the "best" located house or the "top" surgeon when we need an operation.

There was a time when politicians, particularly those in the Liberal Party, talked about self-reliance, deferred gratification and discipline. But such conservatives are long gone. Now the best the Liberal Party has to offer is a form of anti-market paternalism in which we can all enjoy lower taxes, higher incomes, and none of the pain of deferring present consumption in order to make those public and private investments needed to ensure our future prosperity.