The pursuit of tax aware investment management (TAIM) to maximise member outcomes

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Who cares?

Social impact
Australia’s retirement income system and tax revenue generation

Commercial impact
Increasing size of funds under management and compulsory contributions

Regulatory impact
Negotiating competing objectives
Research objectives

1. Evaluate empirically whether trustees of industry superannuation funds are effectively managing taxation for the benefit of members.

2. Examine whether the various opportunities to effectively manage taxation are associated with the variation in the effective tax rates of industry superannuation funds.
Motivation

Concerns were highlighted in the Cooper Review, where tentative estimates suggest costs of tax mismanagement can range from

“5 basis points per annum …up to some 200 basis points per annum on a more holistic basis”¹

The Productivity Commission Review (PC) identified that tax mismanagement is a contributing factor to the erosion of member balances, and it was were highlighted in the Cooper Review, where tentative estimates suggest costs of tax mismanagement can range from

“biggest item to detract from net returns and ultimately member balances”²

¹ Cooper et al., 2010 pg. 87
² Productivity Commission, 2016 pg. 7
Motivation

The PC acknowledge that superannuation taxation is complex, however, cannot draw firm conclusions on whether funds are optimising tax management\textsuperscript{1}.

“The complexity of superannuation taxation makes it difficult to evaluate these differences and the impact they have on member balances, but each type of fund is likely to have advantages and disadvantages.”\textsuperscript{2}

Mackenzie & McKerchar (2014) provide qualitative evidence that discusses a range of practices that Chief Investment Officers (CIOs) adopt referred to as Tax Aware Investment Management (TAIM):

“Active management of taxes of a fund by incorporating tax consequences into the investment process.”\textsuperscript{3}

\textsuperscript{1} Productivity Commission, 2016
\textsuperscript{2} Productivity Commission, 2016 pg. 132
\textsuperscript{3} Mackenzie & McKerchar, 2014 pg. 253
Comparison of media benchmark tax rate (15%) and average ETR

Sivapalan et al
Contributions

Superannuation, TAIM and Practice

• Empirically evaluate the effective management of taxes amongst the funds
• Development of a conceptual framework to further the literature from Mackenzie and McKerchar (2014)
• Assess the impact of legislative amendments to SIS Act.
Research Proposition

1. $RP_1$: Funds employing tax propagation manage tax more effectively than funds not employing tax propagation and have a lower incidence of taxation.

2. $RP_2$: Funds with a higher proportion of My Super accounts are able to manage tax more effectively than funds with a lower proportion of My Super accounts.

3. $RP_3$: Large superannuation funds are more effective in tax management than small funds, with this being reflected in lower ETRs.
Data & research design

- Industry Superannuation funds – 41 Funds in the population during the period of this study 2014 - 2016. (26 Individual funds in the sample)
- APRA fund level superannuation statistics.
- Audited Unabridged Financial Statements – hand collected
- Corporate Governance variables from Annual Reports to members or from disclosures on websites of the funds.
- The unbalanced final sample to test hypotheses is 60 fund years.
## Descriptive Statistics

<table>
<thead>
<tr>
<th>Descriptive All</th>
<th>Obs</th>
<th>Mean</th>
<th>Std Dev</th>
<th>Min</th>
<th>Median</th>
<th>Max</th>
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<td>ETR</td>
<td>60</td>
<td>0.085</td>
<td>0.017</td>
<td>0.045</td>
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<td>CETR</td>
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<td>0.042</td>
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<td>0.087</td>
<td>0.023</td>
<td>0.032</td>
<td>0.091</td>
<td>0.119</td>
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<td>0.188</td>
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<td>0.100</td>
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<td>Chair</td>
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<td>0.502</td>
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<td>1.000</td>
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<td>Accruals</td>
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<td>Held</td>
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<td>0.411</td>
<td>0.264</td>
<td>0.010</td>
<td>0.385</td>
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PRELIMINARY FINDINGS - TAX PROP (HI)

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<th>(75%) Partition</th>
<th>(n)</th>
<th>Mean</th>
<th>min</th>
<th>max</th>
<th>SD</th>
<th>p50</th>
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<td>9.187435</td>
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<td>4.094345</td>
<td>10.1242</td>
<td>1.235154</td>
<td>7.291456</td>
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QUESTIONS & FEEDBACK