Submission to Treasury with respect to the Tax Laws Amendment (Sustaining the Superannuation Contribution Concession) Bill 2013 and the Superannuation (Sustaining the Superannuation Contribution Concession) Imposition Bill 2013

8 May 2013

The Association of Superannuation Funds of Australia Limited – ABN 29 002 786 290
ASFA Secretariat
PO Box 1485, Sydney NSW 2001
T 02 9264 9300 (1800 812 798 outside Sydney)
F 1300 926 484
W www.superannuation.asn.au

*   *   *   *

About ASFA

ASFA is the peak policy, research and advocacy body for Australia's superannuation industry. It is a not-for-profit, sector-neutral, and non-party political national organisation whose aim is to advance effective retirement outcomes for members of funds through research, advocacy and the development of policy and industry best practice.

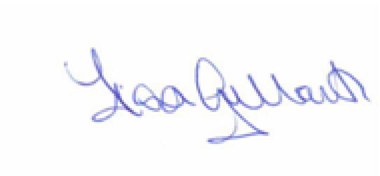
ASFA's focus is on whole of system issues and its core strategies are aimed at encouraging industry best practice, advocating for a system that plays a productive role in the Australian economy and ensuring the industry delivers on its primary purpose of delivering decent retirement incomes.

Our membership - which includes superannuation funds from the corporate, industry, retail and public sectors, and, through its service provider membership, self-managed and small APRA funds - represents over 90 per cent of Australians with superannuation.

*   *   *   *

Should you have any queries regarding the contents of this submission, please do not hesitate to contact me on (03) 9225 - 4021 or 0431 490 240 or fgalbraith@superannuation.asn.au.

Yours sincerely



Fiona Galbraith
Director, Policy

1. <u>Overall Comment</u>

ASFA welcomes the opportunity to provide a submission on the *Tax Laws Amendment (Sustaining the Superannuation Contribution Concession) Bill 2013* and the *Superannuation (Sustaining the Superannuation Contribution Concession) Imposition Bill 2013*.

We maintain our previously advocated position that changes should not be made to the superannuation system in isolation to reduce expenditure or address what is perceived to be an equity issue.

As superannuation is a long-term investment, and preservation precludes members from removing their money from the super system, there is a need for stability and long-term thinking in policy settings to maintain confidence in the system. Without this there is a risk that voluntary contributions into superannuation will to discouraged and instead will be diverted into such things as negatively geared property and shares.

ASFA notes in this context that the $300k amount is not indexed. This will mean that, over time, the real value of $300k will reduce and increasingly will affect more and more members and represent a relatively lower level of income.

Instead, there should be a comprehensive review of the tax system with respect to investments and its interaction with the social security, health and aged care systems.

We are also concerned that - as the tax will not raise a large amount of revenue ($200m in the first year) and will prove expensive for the ATO and funds to administer and collect - this will encourage future governments to reduce the threshold from $300k, which will affect more and more members. As such, it will become less a matter of equity and more a revenue measure.

Notwithstanding this, we have reviewed the draft legislation and provide the following comments.

2. <u>Defined Benefit Funds</u>

The arrangements will be administratively complex and costly for defined benefit funds and will prove difficult to explain to fund members.

2.1. Defined Benefit Contributions

ASFA submits that the preferable option would be to calculate notional contributions on the same basis as are calculated with respect to the excess concessional contributions cap under Div 292. This would be relatively straightforward for the fund to calculate and would mean that funds would be more likely to be able to report by 31 October this year.

Alternate methodology would necessitate considerable volumes of work having to be performed by such professional as actuaries, computer programmers and system testers and would materially increase compliance costs for all defined benefit funds, including those with few or no members likely to trigger the $300,000 threshold. Actuarial fees alone would amount to thousands of dollars, even if there were only one or two defined benefit members left, with low incomes.

Utilising the excess concessional contributions cap methodology would also serve to minimise the risk of confusion among members.

2.2. Accrual of Tax Debt

Under Div 133 of new Part 3-20 *Taxation Administration Act 1953* the amount of Division 293 tax payable with respect to a defined benefit interest is deferred for later payment and included in a debt account maintained by the Commissioner of Taxation.

The exposure draft bill at proposed section 134-15 states: -

> *"(1) If a debt account of yours is in debit at the end of a *financial year, the Commissioner is to debit the account for interest on the amount by which the account is in debit, calculated at the *long term bond rate for that financial year".*

ASFA notes that - if the method to calculate interest is to be the same as that which applies to surcharge debts of unfunded superannuation funds - the interest applied is a full year's interest at the bond rate irrespective of when the Division 293 tax is assessed and added to the debt account. By way of example, if an amount of Division 293 tax is assessed and added to a debt account on 31 December 2013, and 30 June 2014 bond rate is 6%, the interest amount would be a full 6% of the $2000 irrespective of the fact that the liability for tax was only assessed at the 6-month mark.

As it is likely that only unfunded superannuation funds would be aware of the methodology of the surcharge interest calculation it may be appropriate for the ATO to specifically indicate that this is the method which is being applied. Without this, funds would naturally determine the interest with respect to the period from the assessment until year-end (6 months in the example provided) and not for the full year.

Finally, if the interest method to be used is that utilised in unfunded superannuation funds with respect to surcharge debt accounts, the use of the expression "*long term bond rate **for that financial year"*** may be inappropriate and the words "*long term bond rate **as at the end of the** financial year"* should be used.

2.3. End Benefit Cap Calculated Amounts

As the actual value of benefits received from a defined benefit interest can only be known with certainty when the benefit is paid, under section 134-65(2) of the *Tax Administration Act 1953* the annual assessment for Division 293 tax will be based on the notional defined benefit contributions which are determined with respect to the estimated amount of final benefit. The actual benefit received may be less, and sometimes significantly so, than the estimated level of benefit on which the Division 293 tax was based, which means that an individual may, in some cases, be liable for tax despite receiving limited benefits.

To protect individuals from paying amounts of Division 293 tax on estimated employer contributions with respect to benefits which are ultimately not payable, the debt for deferred tax is limited to 15 per cent of the employer-financed component of the benefit which accrued after 1 July 2012.

ASFA notes that – if this concept is retained in the final legislation - "employer financed component of the benefit" will need to be defined.

We note that, while the concept of an "end benefit cap" will provide a reasonable outcome for those members who exceed the $300,000 income threshold every year, it provides very limited, if any, protection for those members who only exceed the $300,000 threshold in some years.

The protection is also inadequate where a member has pre-paid their deferred tax debt.

Accordingly, ASFA submits that a measure should be introduced whereby, if the amount of tax paid exceeds the end benefit cap, the member should be entitled to be paid a refund of the amount by which the tax paid exceeded their end benefit cap, plus interest.

Although the concept of an "end benefit cap" appears relatively straightforward, there is a variety of circumstances where the proposed calculation will be quite complex, including where there has been a family law split or a transfer of the defined benefit to another fund.

Proposed sub-section 134 – 65(2) stipulates that the value of the superannuation interest is to be worked out as at the end of the financial year before the year in which the end benefit becomes payable. One ASFA member has indicated that a preferable approach may be to take the final benefit (as opposed to the previous 30 June benefit), subtract the member financed benefit and then proportion into pre and post 1 July 2012 amounts before applying the 15%. We submit that this approach is worthy of consideration.

ASFA submits that this measure should be reconsidered and the Actuaries Institute consulted to ensure that whatever end benefit cap measure is employed is equitable, both between accumulation and defined benefits and in respect of different defined benefit member scenarios, and is workable for the funds to implement.

If the end benefit cap is utilised, then under proposed new section 134-65(3) it is proposed that the Commissioner may request that a fund must give a notice in the approved form of the end benefit cap for an interest within seven days of the Commissioner making the request.

This is an exceptionally short time frame and ASFA submits that a much more reasonable time frame would be 30 days. It is, of course, always open to the fund to provide the information earlier, however, we submit that seven days is unreasonable for a statutorily imposed deadline with the potential for attendant penalties.

3. When Tax Debt Amount Payable

With respect to defined benefit funds, given the nature of defined benefit interests and the indexation of the debt amount, there is an argument that an alternate mechanism be that the ATO make an annual assessment and the member be able to choose to serve a release authority on any fund which holds a super interest for them at the time of the assessment, not just the defined benefit fund in respect of which the debt arose when the defined benefit becomes payable.

Similarly, there is an argument that the deferral of tax for defined benefit interests could cease when the member's superannuation interest in the defined benefit fund is comprised of an accumulation component, either in full because benefit has crystallised or in part, irrespective of whether or not a payment has been made.

Under proposed new section 293-65, tax amounts are payable by the member within 21 days of assessment. Under proposed section 135-10 the Commissioner must issue release authorities to allow amounts to be released to facilitate payment of liabilities for Division 293 tax, although under proposed section 135-85, funds will have 30 days from the date the release authority is received from the member to release amounts.

While we acknowledge that what is being proposed is broadly consistent with the current rules for release authorities for excess contributions, ASFA submits that these two periods should be aligned, with the period for payment, before interest is payable, being 30 days as well. Provided the member has provided the release authority to their fund and the fund has made the payment within the 30 days no interest should apply.

With respect to defined benefit interests, the deferred tax should not become payable until 30 days after the Commissioner issues an assessment requesting payment – not 30 days after a benefit becomes payable.

Where a MySuper member has a benefit less than the amount in the release authority, the fund will make payment for the full amount and therefore not charge the member an exit fee. As such, there will needs to be an exemption created within the MySuper fee charging rules with respect to this.

Further, there are some defined benefit funds which allow immediate family law splits of defined benefit interests and this does not appear to be an excluded type of payment. This could result in a split to pay a former spouse triggering the ATO to send the member a bill for the debt but as the member's remaining interest is a defined benefit they are unable to access the benefit to make the payment. ASFA submits that family law splits should be excluded from triggering the tax amount being payable.

Furthermore, non-successor fund transfers of defined benefits to another fund - where the original defined benefit has not been crystallised – should also be excluded from triggering payment of the tax debt.

In addition, the payment of an income benefit as a result of a member's temporary incapacity should not trigger payment of the debt.

It appears as though the debt is not extinguished on the death of the member and the liability generally will pass to the estate. If the benefit is paid directly to one or more dependants (as is commonly the case) or a pension is payable, no amount from the super fund will pass to the estate and presumably this means that the debt will need to be paid from any other (non-super) assets in the estate. While generally a person earning more than $300,000 would reasonably be expected to have sufficient assets in their estate to meet the debt, there will be circumstances in which this is not the case, in which case presumably the tax would never be paid.

Finally, section 134-110 requires members with debts to notify the Commissioner when they request a benefit payment and before the benefit is paid. This is unduly onerous and will result in a significant number of instances on non-compliance, triggering unnecessary enforcement action such as penalty notices and fines.

In particular, this obligation appears redundant as the fund is subject to an equivalent requirement under section 134-115 to notify the ATO.

ASFA submits that this section should be removed.

4. Contributions subject to excess contributions tax and temporary residents

ASFA welcomes the fact that contributions subject to excess contributions tax are outside the scope of this measure and that departed temporary residents are able to receive a refund of any tax paid under this measure. This represents an equitable outcome.

ASFA does have a concern, however, about how many refunds will be applied for by departing temporary residents. Proposed section 293-195 states that a former temporary resident must apply for the refund in the approved form. Given this, it is critical that departing temporary residents are made aware of the existence of the refund and the need to apply for it. This is especially the case as all of the current ATO messaging re DASP, as acknowledged in the Explanatory Memorandum at paragraph 2.84, is that it is a final withholding tax and the benefit amount does not need to be included in an income tax return.

5. Definition of "income"

Under proposed 293-20 the definition of "income" utilised for this measure is income for surcharge purposes, as defined in section 995-1 of the *Incomes Tax Assessment Act 1997*, less reportable superannuation contributions plus "low tax contributions" (as defined).

While a lump sum death benefit to a dependent would not be included, as under section 302-60 it is not assessable income, it appears as though the taxable component of a death benefit to a non-dependant would be caught (section 302-140 and 302-145) and some parts of a death benefit income stream may be caught (section 302-85 and section 302-90).

ASFA submits that receipt of superannuation death benefits should be excluded from the definition of income which is counted towards the $300,000 threshold.

ASFA submits that receipt of superannuation death benefits should be excluded from income which is counted towards the $300,000 threshold.

6. Amendment to regulations

6.1. Non-commutable lifetime pensions

It appears as though payment of the debt account will be triggered irrespective of whether the first payment from the defined benefit interest is a lump sum or a pension or a combination of both. There are a number of defined benefit funds which still pay non-commutable lifetime pensions. Accordingly, the SIS regulations will need to be amended to enable such pensions to be commuted to the extent necessary to meet any release authority with respect to deferred Division 293 tax served on the fund by the member.

6.2. Taxation Release Authorities and Preservation Components

ASFA submits that the SIS Regulations should be amended such that a payment made as a consequence of a taxation release authority – be it with respect to the excess contributions tax or this measure - is not required to be taken paid first from unrestricted non preserved and then restricted non preserved then preserved. As this is a tax payable by the member, with respect to concessional contributions made to the fund, it would not be inappropriate for this to be deducted from the preserved component.

++++++++++