



27 October 2014

Manager
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Dear Manager

**TAX AND SUPERANNUATION LAWS AMENDMENT (2014 MEASURES NO. 7) BILL 2014:
EXCESS NON-CONCESSIONAL SUPERANNUATION CONTRIBUTIONS TAX REFORMS**

The Law Council of Australia is pleased to provide comments on Tax and Superannuation Laws Amendment (2014 Measure No 7)n . This submission was prepared for the Law Council by Superannuation Committee of the Legal Practice Section of the Law Council of Australia Section of the Law Council.

The Law Council would be pleased to discuss its submission with the Department. In the first instance, please contact Hanna Jaireth in the first instance at hanna.jaireth@lawcouncil.asn.au

Yours sincerely

**MARTYN HAGAN
SECRETARY-GENERAL**



Law Council
OF AUSTRALIA

Tax and Superannuation Laws Amendment (2014 Measures No. 7) Bill 2014: Excess non- concessional superannuation contributions tax reforms

**Contributions and Accumulations Unit
Personal and Retirement Income Division
The Treasury**

24 October 2014

Submission by the Superannuation Committee of the Legal Practice Section of the
Law Council of Australia

About the Law Council of Australia's Superannuation Committee

The Law Council of Australia is the peak national representative body of the Australian legal profession; it represents some 60,000 legal practitioners nationwide. Attachment A outlines further details in this regard.

This submission has been prepared by the Law Council of Australia's Superannuation Committee (the **Committee**), which is a committee of the Legal Practice Section of the Law Council of Australia.

The Committee's objectives are to ensure that the law relating to superannuation in Australia is sound, equitable and demonstrably clear. The Committee makes submissions and provides comments on the legal aspects of virtually all proposed legislation, circulars, policy papers and other regulatory instruments which affect superannuation funds.

Introduction

The Committee welcomes the reform measures reflected in the *Tax and Superannuation Laws Amendment (2014 Measures No. 7) Bill 2014: Excess non-concessional superannuation contributions tax reforms (Bill)* to address the concerns that have been raised by the Committee and by professional and industry associations over several years about the operation of the excess non-concessional contributions tax rules.

The Committee appreciated the opportunity to discuss the bill with Treasury at the Workshop held in Sydney on 17 October 2014 attended by Committee member Heather Gray. In this Submission, the Committee outlines and expands on a number of issues in relation to the Bill raised by its representative at the Workshop.

Associated earnings

1. The Committee notes that the regime introduced pursuant to the Bill includes the amount of 'associated earnings' in respect of excess non-concessional contributions in the assessable income of a taxpayer. The associated earnings are determined using a proxy rate, which is the lower of a rate worked out under subsection 8AAD(1) of the *Taxation Administration Act 1953 (TAA)* (i.e. the general interest charge rate) using the formula set out in item 31 of the Bill (new section 97-30(1) of Schedule 1 TAA) and a rate determined by the Minister by legislative instrument under proposed section 97-30(2) TAA. The associated earnings are determined for the period from the first day of the relevant contributions period through to the day on which the Commissioner makes the first excess non-concessional contributions determination for the contributions year.
2. The Committee raises the following issues regarding associated earnings:
 - The use of the general interest charge rate is inappropriate, and has the potential to result in a punitive tax liability where returns within relevant superannuation fund/s have been low for the relevant period. Given that the reforms are not intended to create effective penalties for taxpayers who find themselves in a position where they have excess non-concessional contributions, and the Budget announcement referred simply to 'associated

earnings', the Committee considers that the method of calculation should be one more likely to have broad consistency with market returns.

- The Committee queries why the associated earnings are not to be determined in a manner similar to the determination of excess concessional contributions charge under Division 95 of Schedule 95 TAA. In the Committee's view, this would produce a result more consistent with the objective of the reforms. It would also simplify the explanation of the regime for APRA-regulated funds, which need to make disclosures regarding tax matters to their members. An explanation that needs to cover quite different approaches in respect of excess concessional and excess non-concessional contributions will inevitably be more complex and potentially confusing for those members than would be the case if the approach were to be substantially the same. It is noted that the Minister will have power to determine an alternative proxy rate that is lower than the general interest charge. However, there is no guidance in either the Bill or the draft Explanatory Memorandum (**EM**) regarding the circumstances in which it is expected that the Minister will exercise that power. Some such guidance should be included. For example, is it intended that the Commissioner would exercise this power whenever average rates of return within the superannuation system fall below the level of the general interest charge?
- The Committee notes the statement at paragraph 1.33 of the EM that an approximation is used for associated earnings to avoid the complexity that would be imposed on individuals and superannuation providers if calculations of actual earnings amounts were to be required. However, the Commissioner also notes that self managed superannuation funds are generally readily able to determine actual earnings attributable to members. It may therefore be appropriate to allow taxpayers who have excess non-concessional contributions arising in circumstances where the released amount will come from an SMSF to elect to use an actual earnings rate. Integrity could be maintained by, for example, requiring that rate to be supported by an actuarial certificate.
- If an option to use an actual earnings rate is to be included in the Bill, and this is to apply in relation to APRA-regulated funds as well as to SMSFs, provision will need to be included allowing the trustee of an APRA-regulated fund to opt in or out of providing actual earnings rates without liability to members.
- There is no provision in the Bill for an offset of tax paid on earnings in respect of excess non-concessional contributions while those amounts are held within a superannuation fund. The imposition of additional tax on these earnings (and at a proxy rate which is likely to be higher than the actual earnings rate) effectively creates double taxation on these earnings (unless of course the relevant earnings within the fund qualify as exempt current pension income). The Committee queries whether this is intended (noting that this was not highlighted in the Budget announcement), and is strongly of the belief that, as a matter of principle, double taxation should not be incorporated within the taxation system.
- The Committee notes, as mentioned above, that associated earnings are to be calculated for a period running from the first day of the relevant contributions year. As a practical matter, the experience of Committee members suggests that non-concessional contributions are more likely to be made towards the end of a year rather than at the beginning. In any event, this approach will

inevitably mean that in many instances taxpayers incur tax on notional earnings that were not in fact received by them. The Committee suggests that a fairer approach would be to use as a start date a date halfway through the contributions year, or to allow the taxpayer to elect to nominate an actual contributions date where this can be established to the Commissioner's satisfaction.

Release authorities

1. Item 14 of the Bill provides for the insertion of new section 96-7 into Schedule 1 TAA.
 - (a) Section 96-7(1) provides for three options - the taxpayer may elect to release 'the total amount stated in the determination', elect not to release 'that amount' because the value of their superannuation interests is nil; or elect not to release 'that amount' for some other reason. The Committee considers it should be made clear that references to 'that amount' are to 'the total amount stated in the determination', and that therefore an election cannot be made to release a part only of a determined amount.
 - (b) Section 96-7(2) refers to the situation in which an amended determination is issued. In this case, any new elections are to be made as if, where the taxpayer made an election for 'each earlier excess non-concessional contributions determination received for the financial year', the total amount were reduced by the sum of any amounts paid to the taxpayer in response to release authorities issued in relation to earlier determinations, or otherwise by the total amount in the most recent earlier determination.
 - (i) The Committee thinks that in 'each earlier excess non-concessional contributions determination received for the financial year' the word 'each' should be replaced with 'any' to avoid the result that the taxpayer would have to have made an election in response to every earlier determination.
 - (ii) There also seems to be a timing issue here. If an earlier determination was issued and the time allowed to make the election has not yet passed, it seems that the taxpayer is precluded from making such an election, despite being within time, if an amended determination has since been issued. This seems to be unintended, and in the Committee's view the provision should be amended to avoid this result.
 - (iii) In any event, it is unclear why a taxpayer should be precluded from making an election in respect of the total amount of a new determination even if they did decide not to elect to release the amount in an earlier determination. The Committee considers that greater flexibility should be allowed here.
 - (c) Section 96-7(5) deals with the case in which the Commissioner gives a notice that a superannuation provider did not pay in relation to a release authority. It should be made clear that this relates to partial and total non-payment, and that the further election allowable is for the reduced amount in the event that a partial release has already occurred.

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2. Item 17 of the Bill provides for the insertion of new section 96-12 into Schedule 1 TAA.
 - (a) Section 96-12(1) provides that the 'Commissioner may issue a release authority' where a taxpayer makes a valid election to release the amount stated in an excess non-concessional contributions determination from their superannuation interests. The Committee considers that it should be mandatory for the Commissioner to issue a release authority in this circumstance and that therefore 'may' should be replaced with 'must'.
 - (b) In section 96-12(1), the Committee queries rather paragraphs (a) and (b) should be separated by 'or' rather than 'and'. It should also be made clear that the Commissioner can issue a release authority to a combination of identified superannuation providers and other providers chosen by the Commissioner (assuming this is the intention).
 3. Item 19 provides for the insertion of new sections 96-20(1A) and (1B) into Schedule 1 TAA.
 4. Section 96-20(1A) requires a superannuation provider issued with a release authority to make payment to the individual within 7 days after the release authority is issued.
 - (a) The Committee suggests that the timeframe needs to take account of delays between the issue of a release authority and its receipt by a superannuation provider.
 - (b) In any event, the Committee suggest that 7 days is too short a period, bearing in mind that the provider may need to make internal decisions about matters including the interests from which the amount will be released, and in the case of some types of interests (e.g. pensions, defined benefit) may need to take advice as to whether a release can be made. The Committee suggests that 14 or 21 days would be a more appropriate period (and that the date for payment of an assessment in respect of tax on the associated earnings should be aligned accordingly).
 - (c) Regardless of the time allowed in the usual case, the Committee considers that provision should be included to give the Commissioner to allow a longer period. There will be circumstances in which, for example, an illiquid asset will need to be sold in order to satisfy a release authority, such as where the members of a SMSF have acquired real property with the relevant contributions.
 - (d) These comments regarding timing apply equally to proposed new section 96-25.
 - (e) The provision should also be amended to make it clear that a superannuation provider must release the relevant amount even if outside of the statutory period. In other words, failure to meet the statutory timeframe should not have consequences other than the imposition of a penalty. (A similar issue arose in respect of Regulation 7.04(4) of the *Superannuation Industry (Supervision) Regulations 1994*, which requires certain amounts to be returned within 30 days. It was unclear whether a fund that missed this deadline was still required (or indeed allowed) to return the relevant amounts.)
 5. As regards proposed section 96-20(1B):

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- (a) The Committee notes that under the released amounts are to be paid from the tax free component of the individual's superannuation interests. The Committee considers it to be inequitable that this rule should apply to the portion of the released amount that reflects the associated earnings, and suggests that this portion should be paid from the taxable component (or that the provider should have the option of paying this portion from the taxable component).
- (b) The Committee suggests that the EM be amended to make it clear that the superannuation provider is entitled to make a decision as to the interests of the individual from which the amount required under the release authority will be paid.
6. Item 27 provides for the insertion of new section 96-40 into Schedule 1 TAA. There are drafting errors in this provision, which in part assumes incorrectly that amounts might be released to the Commissioner under a release authority arising from an election under section 96-7(1)(a).

Nil superannuation interests

Item 3 provides for the insertion of new section 292-467 into the *Income Tax Assessment Act 1997*. This deals with the direction by the Commissioner that the value of an individual's superannuation interest is nil. The Committee recommends that it be made clear that the Commissioner may make such a direction even if not satisfied that the value of the individual's superannuation interest is in fact nil, in circumstances where there would otherwise be an inequitable result. For example, if an individual had a very small amount still held within an illiquid option within a superannuation fund, with a low probability that such amount would ever become available to be released, it would be inequitable if such individual were to become liable to pay excess non-concessional contributions tax.

The Committee would welcome the opportunity to discuss its submission further and to provide additional information in respect of the comments made above.

Attachment A: Profile of the Law Council of Australia

The Law Council of Australia exists to represent the legal profession at the national level, to speak on behalf of its Constituent Bodies on national issues, and to promote the administration of justice, access to justice and general improvement of the law.

The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian State and Territory law societies and bar associations and the Large Law Firm Group, which are

known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar
- The Large Law Firm Group (LLFG)
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of approximately 60,000 lawyers across Australia.

The Law Council is governed by a board of 23 Directors – one from each of the constituent bodies and six elected Executive members. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive members, led by the President who normally serves a 12 month term. The Council's six Executive members are nominated and elected by the board of Directors.

Members of the 2014 Executive are:

- Mr Michael Colbran QC, President
- Mr Duncan McConnel President-Elect
- Ms Leanne Topfer, Treasurer
- Ms Fiona McLeod SC, Executive Member
- Mr Justin Dowd, Executive Member
- Dr Christopher Kendall, Executive Member

The Secretariat serves the Law Council nationally and is based in Canberra.