A Plan to Simplify and Streamline Superannuation

Outcomes of Consultation

5 September 2006

INTRODUCTION

On Budget night the Government released a consultation paper which outlined its plan to reform Australia's superannuation system. The detailed outline of *A Plan to Simplify and Streamline Superannuation* described the changes and how the new system would operate.

This attachment announces the Government's response to the consultation and consideration of the plan. The attachment uses similar headings to those used in the detailed outline and refers to the relevant page numbers of that document to facilitate cross referencing.

OUTLINE OF PROPOSAL

Under the proposals described in the detailed outline, from 1 July 2007:

- Superannuation benefits paid from a taxed source either as a lump sum or as an income stream such as a pension, would be tax free for people aged 60 and over.
  - Benefits paid from an untaxed source (mainly affecting public servants) would still be taxed, although at a lower rate than they are now for people aged 60 and over.
- RBLs would be abolished.
- Individuals would have greater flexibility as to how and when to draw down their superannuation in retirement. There would be no forced payment of superannuation benefits.
- The concessional tax treatment of superannuation contributions and earnings would remain. Age-based restrictions limiting tax deductible superannuation contributions would be replaced with a streamlined set of rules.
- The self-employed would be able to claim a full deduction for their superannuation contributions as well as being eligible for the Government co-contribution for their post-tax contributions.
- The ability to make deductible superannuation contributions would be extended up to age 75.
- It would be easier for people to find and transfer their superannuation between funds.

To increase further the incentives to save for retirement, from 20 September 2007 the pension assets test taper rate would be halved to $1.50 per fortnight for every $1,000 of assets above the assets test free area.

The superannuation preservation age would not change. The preservation age is already legislated to increase from 55 to 60 between the years 2015 and 2025. People would still be able to access superannuation benefits before the age of 60, although they would continue to be taxed on their benefits under new simplified rules.

GLOSSARY

This attachment refers to the same terms as explained in the glossary to the detailed outline.

Taxation of benefit payments

Note: the taxation of benefits paid from an untaxed source is dealt with on page 20.

Key Points

- Superannuation benefits paid from a taxed source either as a lump sum or pension will be tax free when paid to people aged 60 and over.
- Superannuation benefits paid before age 60 will be taxed in a similar manner as they are now.
- RBLs for superannuation will be abolished.
- The current concessional tax treatment of invalidity payments will be extended to the self-employed.

Rules for benefits paid to individuals aged 60 and over (page 12)[1]

Lump sums

From 1 July 2007, all lump sum benefits paid from a taxed source to an individual aged 60 or over will be tax free. There will be no RBL.

Pensions

All pension payments from a taxed source will be tax free when paid to individuals aged 60 or over. This will also apply to pensions which commenced before 1 July 2007. There will be no RBL.

Reporting

Individuals will not need to include lump sum superannuation benefits and superannuation pensions from a taxed fund made after 30 June 2007 in their tax returns.

Superannuation funds will not need to report benefit payments made after 30 June 2007 to the ATO for RBL purposes.

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[1] Headings and page numbers are references to those in the detailed outline *A Plan to Simplify and Streamline Superannuation.*

RULES FOR BENEFITS PAID TO INDIVIDUALS AGED UNDER 60 YEARS (PAGE 13)

Lump sums

Lump sums will have two components — an exempt component and a taxable component (there are different rules for payments from an untaxed source).

- The exempt component will be tax free. The exempt component will comprise: the pre-July 1983 component, the CGT exempt component, the post-June 1994 invalidity component, the concessional component and undeducted contributions.

- The taxed component (the current post-June 1983 component and the non-qualifying component) will be tax free up to the low-rate threshold and taxed at a maximum rate of 15 per cent above the threshold. For those aged under 55, this component will be taxed at a maximum rate of 20 per cent. This is the same treatment as currently applies to the post-June 1983 component.

  – The low rate threshold will be set at $140,000 on 1 July 2007 and indexed to Average Weekly Ordinary Times Earnings (AWOTE) in $5,000 amounts.

Calculating the pre-July 1983 component

Funds will be required to calculate a pre-July 1983 amount. This will be calculated on the value of the benefits as at 30 June 2007, using the existing legislative formulae, with the lesser amount to be crystallised. Superannuation funds will have until 30 June 2008 to calculate this amount. Once calculated, this amount will become a fixed component that will not change in the future and will form part of the new exempt component.

There will be no crystallisation of the pre-July 83 component of employer ETPs. The pre-July 83 component will continue to be calculated by the employer upon termination of employment.

Pensions

Pension payments for individuals aged under 60 will continue to be taxed under current arrangements, although consistent with the simplification of taxation of lump sum payments, tax will be lower in some cases.

Pensions commenced on or after 1 July 2007, which would currently qualify for a pre-July 1983 component will have this included in the exempt component of the pension. The current arrangements for calculating the deductible amount of a pension will remain for pensions that commenced prior to 1 July 2007.

The full superannuation pension rebate of 15 per cent will apply to all pensions paid from a taxed fund if the individual is aged 55 to 59 years.

Once the pension recipient turns 60, their pension will be tax free.

Reporting —arrangements

Individuals aged under 60 will still be required to report details of lump sums and pensions in their tax return.

Benefit payments made after 30 June 2007 will no longer be reported to the ATO by superannuation funds for RBL purposes.

Proportional drawdown of benefits

From 1 July 2007, when any part payment of a superannuation benefit is made, the benefits will be considered to include both exempt and taxable components with the relevant portions of each reflecting the proportions such components make up of the total benefit. This will apply to both lump sums and pensions. This will support the plan's objectives to encourage higher participation in the workforce. Existing pensioners will retain the current 'deductible amount' on their pension until they reach age 60 when benefits become tax free in any case.

DEATH BENEFITS (PAGE 15)

The current superannuation system provides favourable tax treatment to death benefits paid to a dependant. The plan continues with this treatment of death benefits. Lump sum death benefit payments will be tax free if paid to a dependant. The definition of dependant will remain as currently defined in the *Income Tax Assessment Act 1936* (paragraph (b) in subsection 27A(1)). The taxable component of a lump sum paid to a non-dependant will be taxed at 15 per cent (as is currently the case for the post-June 1983 taxed element).

The taxation of a death benefit paid as a reversionary pension will depend on the age of the primary and reversionary beneficiary. If the primary beneficiary was aged 60 or over at the time of death, then payments to the reversionary beneficiary will be tax exempt. If the primary beneficiary was under age 60 at the time of death, the pension will continue to be taxed at the reversionary beneficiary's marginal tax rate (less any deductible amount and pension rebate) unless, or until, the reversionary beneficiary is aged 60 or over, in which case it will be tax exempt.

Death benefits will be able to be paid as a pension to a dependant if the member dies before commencing a pension. These pensions will be taxed in the same way as a reversionary pension.

Death benefits will be able to be paid as a pension to a dependant child, although when the child turns 25 the balance in the fund will have to be paid as a lump sum (tax free) unless the child was permanently disabled.

A pension will not be able to revert or be paid to a non-dependant on death; rather, death benefit payments to non-dependants will have to be made as a lump sum.

TEMPORARY RESIDENTS (PAGE 16)

People who enter Australia on an 'eligible temporary resident visa' and who later permanently leave Australia can claim any superannuation they have accumulated. The payment is subject to withholding tax.

Reflecting the new simplified ETP components, the rates for benefits from a taxed source will be:

- exempt component — 0 per cent; and
- taxable component — 30 per cent.

In practice, this is no change to the current system. If the payment is from an untaxed source, it will continue to be taxed at 40 per cent.

INVALIDITY PAYMENTS

Many submissions sought clarification of the treatment of invalidity benefits under the plan. It is not intended to change the current treatment of these benefits.

Benefits which are paid on the permanent disablement of the member will be eligible for a 'post-June 94 invalidity component' on the part of the benefit taken as a lump sum or a 15 per cent pension offset if taken as a pension. Once the person is aged 60 or above these benefits will be tax free.

The Government will extend eligibility for a 'post-June 94 invalidity component' to the self-employed from 1 July 2007.

Benefits which are paid on the temporary disablement of the member (such as salary continuance benefits) are regarded as 'replacement of income' benefits rather than 'retirement income' benefits. Therefore, these benefits will continue to be treated as income of the member regardless of their age. Funds will continue to provide relevant information to the member to include these benefits in their tax returns.

PAYMENT RULES SIMPLIFIED

Key Points

- The rules for when individuals can voluntarily choose to access their superannuation will not change — that is, individuals will still be able to access their superannuation once they reach preservation age and are able to take their benefits, and from age 65 even if they have not retired.
- An individual will not be compelled to draw down their superannuation once they reach a particular age. They will be free to draw on it as and when they want.
- Pensions will continue to receive favourable tax treatment. However, the rules defining a pension will be simplified.
  - If a person chooses to take a pension, they will be able to take out as much as they like when they like, provided a minimum amount is taken each year.

WHEN BENEFITS CAN, OR MUST, BE PAID (PAGE 19)

Voluntary withdrawal

The preservation arrangements will not change. The preservation age is already legislated to increase from 55 to 60 between the years 2015 and 2025. Members will still be able to take their superannuation once they have reached preservation age and are eligible to take their benefits or once they reach age 65.

Compulsory withdrawal abolished

The requirement for compulsory payment of benefits to members over age 65 who do not meet the current work test, and compulsory payment from age 75, will be removed. This will take effect from 10 May 2006.

SIMPLIFYING PENSION RULES (PAGE 20)

Replacing multiple rules for multiple types of pensions with a simple set of rules

Under the new arrangements, all pensions that meet simplified minimum standards will be taxed the same on payment. Earnings on assets supporting these pensions will remain tax exempt.

Pensions that meet existing rules and commenced before 1 July 2007 will be deemed to meet the new minimum standards.

The new pension standards

The new minimum standards for pensions will require:

- payments of a minimum amount to be made at least annually, allowing pensioners to take out as much as they wish above the minimum (including cashing out the whole amount);
- an amount or percentage of the pension cannot be prescribed as being left-over when the pension ceases; and
- that the pension can be transferred only on the death of the pensioner to one of their dependants or cashed as a lump sum to the pensioner's estate.

The payment rules will specify minimum limits only. No maximum will apply, with the exception of pensions which are commenced under the transition to retirement condition of release which are limited to 10 per cent.

Guaranteed lifetime pensions

Guaranteed lifetime pensions provided on an arm's length basis that meet relevant existing requirements will continue to be acceptable.

Pension payments

Individuals will be able to choose the amount they take from their pension each year. A minimum amount will be required to ensure that the capital is generally drawn down over time. The minimum pension payments are set out below.

Indicative minimum annual pension payments

Age	Per cent of account balance
55 — 64	4
65 — 74	5
75 — 84	6
85 — 94	10
95 +	14

TRANSITION TO RETIREMENT (PAGE 23)

As a consequence of the new pension rules, the transition to retirement rules will be amended to accommodate pensions that meet the new minimum standards.

From 1 July 2007, pensions commenced under the transition to retirement condition of release will allow no more than 10 per cent of the account balance (at the start of each year) to be withdrawn in any one year. The existing non-commutability rules for pensions purchased under the transition to retirement measure will continue to apply. Pensions commenced prior to

1 July 2007 which complied with the relevant rules for the transition to retirement measure at the time will be deemed to satisfy the proposed requirements.

Benefits not withdrawn (page 24)

There will be no compulsory cashing rules under the new arrangements. These changes will allow a person to keep their benefits in a fund indefinitely.

Where a person chooses not to draw down on their fund assets as a pension, then earnings on these assets will be subject to tax as assessable income of the fund at 15 per cent.

Commutation of complying pensions

Under the existing superannuation system, a person can gain access to a higher RBL and/or a pension assets test exemption if they take their benefits as a complying income stream. To gain access to these concessions the person has agreed to give up their right to access their capital.

The plan did not mention how these pensions would be treated under the new system. During consultation on the plan, the Government was made aware of the potential detrimental impact on members and product providers of allowing commutation of guaranteed income pensions. These pensions make up the majority of complying pensions that are currently provided. Various suggestions were made to allow all complying pensions to be commuted provided people with a guaranteed pension were made aware of the potential high cost to them of commuting such a pension, or restricting commutation to non-guaranteed complying pensions such as term allocated pensions.

After consideration of the submissions, the Government agrees that allowing commutation of guaranteed complying pensions would result in potential risks to members and product providers of guaranteed complying pensions. To restrict commutation to non-guaranteed complying pensions would provide preferential treatment to these people even though the decision to take either product was made on a similar basis. The Government therefore does not intend to increase the ability for people to commute a complying pension.

Treatment of existing allocated pensions

Existing allocated pensioners will be allowed to transfer to the new pension products from 1 July 2007 without the need to commute their existing pension. This will save these people the potential cost of moving to the new pension if they had to commute their existing pension to commence a new pension.

SIMPLIFIED CONTRIBUTION RULES

Key Points

- Concessional deductible contributions to superannuation will be limited to $50,000 per person per annum. These contributions will be taxed at 15 per cent.
  - A five year transitional period will apply for people who are aged 50 and above to allow those planning to retire soon to make concessional contributions of $100,000 a year.
- Employers will be able to claim a full deduction for all contributions to superannuation on behalf of individuals under the age of 75. The Superannuation Guarantee will continue to apply only until age 70.
- The personal deduction eligibility rule will be simplified by making it consistent with the rule that currently applies for the Government co-contribution.
- Personal superannuation contributions from an individual's post-tax income (known as undeducted contributions) will continue not to be taxed when contributed and may be eligible for the Government co-contribution (as currently). These contributions will be limited to $150,000 per annum.
  - People under age 65 will be able to bring forward two years of contributions and make a larger contribution of $450,000.
  - Transitional arrangements will apply between 10 May 2006 and 30 June 2007.
- All contribution limits in the plan (except those related to transitional arrangements) will be indexed in $5,000 amounts.

TAXATION ARRANGEMENTS – DEDUCTIBLE CONTRIBUTIONS (PAGE 26)

The age-based limits on deductible contributions will be abolished. A limit on concessional deductible contributions of $50,000 per person per annum will apply from 1 July 2007. These contributions will be taxed at 15 per cent. The $50,000 threshold will be indexed to AWOTE but will only increase once the increase in the indexed amount is greater than $5,000[2]. This will make it easier for people to understand how much concessional contributions they can make each year.

Where the ATO identifies that a person's deductible contributions have exceeded $50,000 in a financial year, the amount in excess of $50,000 will be effectively taxed at the top marginal tax

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[2] Indexation will be calculated on the base amount of $50,000. For example, when the amount becomes $55,000, indexation will be calculated on the non- rounded amount.

rate plus Medicare levy (an additional 31.5 per cent on top of the original 15 per cent paid by the fund).

The new threshold will apply per person, irrespective of the number of employers contributing on behalf of the person.

The current work test of 40 hours in a 30 day period for contributions made by people aged 65 to 74 will continue.

Application to funded defined benefit schemes

The $50,000 cap will apply to contributions made to a funded defined benefit scheme (except for amounts paid into constitutionally protected funds, which are exempt from tax).

For the purposes of determining whether the $50,000 cap has been exceeded by members of such schemes, the 'notional taxable contributions' will be added to any other deductible contributions for each employee. The definition of 'notional taxable contributions' will be determined through further consultation.

Given the unique nature of defined benefit schemes, and the difficulty for members to reduce their contributions, a transitional arrangement will apply to members of these schemes. Existing members of defined benefit schemes (as of 5 September 2006) with notional contributions above the concessional contribution cap will be deemed as having contributions made at the maximum level of the cap for the individual. This arrangement will no longer apply if the scheme amends their rules to increase member benefits.

Treatment of late contributions

Some superannuation funds finance their benefits by making large one-off contributions. The trustee of the fund, with the consent of the contributor, can then elect for these contributions not to be taxable. Some funds also allow their members to elect whether their benefits are paid from a taxed or untaxed source. Where taxed benefits are paid, the concessional cap will be applied on the basis of the notional contributions for each year. Members of new schemes will be unable to elect whether their benefits are paid from a taxed or untaxed source.

ADMINISTRATIVE ARRANGEMENTS FOR CONTRIBUTIONS TAX (PAGE 27)

Superannuation funds, except those that are untaxed, will report to the ATO all taxable contributions (including notional taxable contributions) made for the benefit of an individual.

It was proposed that any additional liability for tax on contributions over $50,000 per annum would be determined in respect of an individual but levied on superannuation funds. Following consultation on the plan, the Government has decided that any additional liability for tax will be levied on the individual. The individual will be able to elect for their superannuation fund to release monies to pay the tax. The ATO will be able to reduce the amount of excess contributions subject to tax in the event of inadvertent breaches of the cap.

AGE-BASED LIMITS AND DEDUCTION RULES (PAGE 28)

Employers

Employers will be able to claim a full deduction for all contributions to superannuation funds made on behalf of their employees under age 75.

Self-employed

Contributions made by the self-employed will be treated in the same way as contributions made by employers for the benefit of employees. Superannuation contributions will be eligible for a full deduction until age 75.

Personal deduction eligibility

The rule that determines a person's eligibility to claim a deduction for personal contributions will be simplified. The test will be changed so that it will only determine how much of a person's assessable income and reportable fringe benefits is attributable to employment as an employee, mirroring the test currently used for determining eligibility for a Government co-contribution.

A person who wishes to claim a tax deduction for a superannuation contribution will need to notify their superannuation fund by the time they lodge their income tax return, or the end of the following financial year after the contribution was made, whichever is earlier. This notification cannot be varied after this time. This will ensure that the ATO will have the relevant information to count the contribution against the relevant cap and to determine eligibility for a co-contribution.

Transitional arrangements

A transitional period will apply which will allow people aged 50 and over to make up to $100,000 of concessional contributions without breaching the cap. This period will apply in the financial years of 2007-08 to 2011-12. A person who turns 50 during that period will be able to take advantage of the transitional arrangements. For example, a person who turns 50 on 1 January 2010 will be able to make $100,000 of concessional contributions in each of the 2010-2011 and 2011-12 financial years. The $100,000 threshold will not be indexed.

From the 2012-13 financial year, the maximum amount of contributions taxed at 15 per cent will revert back to the indexed $50,000 amount.

UNDEDUCTED CONTRIBUTIONS (PAGE 30)

The removal of benefits tax and RBLs will increase the concessions provided to superannuation. These changes, in conjunction with the tax exempt status of superannuation pension assets, will make superannuation an attractive vehicle in which to retain assets to avoid paying tax. There

will also be an incentive for high-wealth individuals to transfer large amounts of assets currently held outside superannuation to the concessionally taxed superannuation system.

To ensure the concessions are targeted appropriately, a cap of $150,000 a year (this will remain at three times the level of the cap on concessional contributions and will increase as the concessional cap moves with indexation) on the amount of post-tax superannuation contributions a person can accrue will apply. To accommodate larger contributions, people under age 65 will be allowed to bring forward two years of contributions. For example, a person under age 65 would be able to make $450,000 in the 2007-08 financial year but will then be unable to make further post-tax contributions until the 2010-11 financial year.

From 1 July 2007, once a person turns age 65 they will be able to make $150,000 of post-tax contributions each financial year provided they satisfy the work test. This will ensure that people will not inadvertently breach the cap by not meeting the work test in the future two years. To simplify the operation of the cap, people aged 63 and 64 who contribute $450,000 will not be required to meet the existing work test in the two years after they make the contribution. The current rules prohibiting contributions by people aged 75 and over will remain.

Refund of excessive contributions

It was proposed to require contributions in excess of the cap to be returned to the individual. In addition, any earnings on that amount were to be taxed at the top marginal tax rate. Following consultation, the Government will not proceed with this proposal. Instead, contributions in excess of the cap will be taxed at the top marginal tax rate (plus Medicare levy). The liability for this tax will be levied on the individual who will nominate a superannuation fund to release monies to pay the liability. The balance of the excess contribution will be able to remain in the fund.

To limit inadvertent breaches of the cap, superannuation funds will be prohibited from accepting contributions in excess of maximum allowable post-tax contributions in a year (that is, $450,000 for people aged under 65). The ATO will have the discretion to reduce the amount of excess contributions subject to the tax if genuine inadvertent breaches arise. Individuals who make contributions in excess of the transitional limits outlined below will be able to withdraw these amounts without penalty prior to 1 July 2007.

Administration

Currently, superannuation funds report the amount of post-tax contributions to the ATO. The ATO will use this information from the funds to determine if a person has exceeded the annual cap.

Exemptions to the cap

The proposed plan indicated that the Government would consider exemptions to the cap. Contributions above the cap will be allowed in the following circumstances:

- the proceeds from the disposal of assets that qualify for the small business capital gains tax (CGT) exemptions (that is, the 15-year exemption and the $500,000 retirement exemption) up to a lifetime limit of $1 million (indexed). This will also apply to assets that would have qualified if they were not pre-CGT assets or if disposed after the permanent disablement of the owner including where the asset was owned for less than 15 years; and

- the proceeds from a settlement for an injury resulting in permanent disablement.

Transitional arrangements

During the consultation period people requested that transitional arrangements be put in place for situations where a person has intended to make contributions above $450,000. There will be a transitional cap of $1 million for post-tax contributions made between 10 May 2006 and 30 June 2007. This will be available to all individuals eligible to contribute to superannuation in the relevant year and will include any contributions already made during that period. The annual cap on post-tax contributions of $150,000, and the ability to make larger contributions of up to $450,000, will commence on 1 July 2007.

Examples

Bert is 55 years old and made post-tax contributions of $150,000 between 10 May 2006 and 30 June 2006 and $450,000 in July 2006. Under the transitional arrangements, Bert can contribute a further $400,000 before 1 July 2007. From 1 July 2007, Bert can contribute $450,000 (and make no further contributions until 1 July 2010), or make annual post-tax contributions of $150,000 per annum.

Angelo is 63 and is planning to sell his family business, which he has operated for more than 15 years, in July 2008. Angelo will be able to contribute $1 million to superannuation from the proceeds of the sale, and a further $450,000 as the maximum post-tax contribution. He will not be permitted to make further post-tax contributions until 1 July 2010.

Angelo's spouse Anna is 65 years old, has no superannuation and has jointly operated the family business with Angelo for the past 15 years. Anna will be able to contribute $1 million to superannuation from the proceeds of the sale of the business. As Anna is aged 65, Anna must meet a work test each year to contribute to superannuation and can make a maximum post-tax contribution of $150,000 per annum.

Contributions included in the post-tax contributions cap

The cap will generally apply to all post-tax contributions made on behalf of an individual. For example, contributions made directly by a person into their spouse's account to qualify for the spouse contributions rebate will be counted against the receiving spouse's cap.

Deductible contributions above the concessional cap will also count towards the post-tax contributions cap. This will ensure people cannot circumvent the post-tax cap by making excessive concessional contributions.

The Government co-contribution will not be included in the cap.

OTHER TAXABLE CONTRIBUTIONS (PAGE 31)

Transfers from overseas superannuation funds

Where a superannuation benefit is paid from an overseas fund more than six months after the individual becomes an Australian resident, a tax liability may arise. The tax liability arises in respect of an amount (the taxable amount) which reflects earnings on the overseas superannuation while the individual was an Australian resident.

- Where the benefit is paid directly to the individual, the taxable amount is included in their assessable income and taxed at their marginal tax rate.
- Where the benefit is transferred to an Australian superannuation fund, the member can elect to have the taxable amount instead treated as a taxable contribution in the Australian fund (and therefore subject to the 15 per cent tax on contributions).

It is proposed that where an individual elects for the taxable amount to be treated as a taxable contribution, then the taxable amount will remain taxed at the flat rate of 15 per cent when contributed to superannuation. This is appropriate as the taxable amount represents earnings on overseas superannuation during the relevant period. These earnings would have been taxed at 15 per cent if they had been in the Australian superannuation fund.

Other benefits (that is, the amount of the transfer exceeding the taxable amount mentioned above) will be regarded as post-tax contributions and count against the post-tax contributions cap.

Transfers from untaxed schemes

Transfers of untaxed benefits from an untaxed scheme into a taxed fund are currently subject to contributions tax when paid into the fund. This will generally continue. New withholding arrangements will apply to the transferring fund (the untaxed scheme) when transferring a benefit. These new arrangements are discussed in the untaxed Schemes section of this paper.

CONTRIBUTION INCENTIVES FOR THE SELF-EMPLOYED

Key Points

- The self-employed (and other eligible persons) will be able to claim a a full deduction for all personal superannuation contributions until age 75.
- Eligible self-employed persons will have access to the Government co-contribution scheme.

AGE-BASED LIMIT AND DEDUCTION RULES (PAGE 33)

From 1 July 2007, the self-employed (and other persons who are currently eligible for a deduction) will be eligible to claim a full deduction for their superannuation contributions up to age 75.

EXTENSION OF THE GOVERNMENT CO-CONTRIBUTION SCHEME TO THE SELF-EMPLOYED (PAGE 34)

The Government co-contribution scheme will be extended to the self-employed, effective from 1 July 2007 provided they satisfy the existing eligibility criteria for the co-contribution.

To provide for the self-employed, income will be determined by adding the assessable income of an individual (including any reportable fringe benefits, if applicable) and then reducing that amount by their expenses incurred in carrying on a business.

Age pension arrangements

Key Points

- The pension assets test taper rate will be halved from 20 September 2007 so that pension recipients only lose $1.50 per fortnight (rather than $3) for every $1,000 of assets above the relevant threshold.
- The assets test exemption for 'complying' income streams will be removed for income streams purchased on or after 20 September 2007.
- There will be no change to the income test arrangements.

Pension assets test (page 37)

The pension assets test taper rate will be halved from 20 September 2007 so that recipients only lose $1.50 per fortnight (rather than $3) for every $1,000 of assets above the relevant threshold.

This will apply to the following payments:

- Age and service pensions;
- Disability support pension;
- Carer payment;
- Wife pension;
- Widow B pension; and
- Bereavement allowance.

Abolition of the 50 per cent assets test exemption for 'complying' income streams (page 38)

The current 50 per cent assets test exemption for purchased 'complying' income streams will be removed from 20 September 2007. This change will only apply to income stream products purchased on or after 20 September 2007 and will not affect the assets test treatment of income streams purchased before this date.

Pension Income Test

The current income test treatment of superannuation pensions will remain unchanged. Income streams with a term of greater than five years are assessed under the income test on the basis of the gross annual income from the product reduced by an annual allowance for return of capital.

Income streams with a term of less than five years are assessed under the social security deeming rules.

OTHER MEASURES

Key Points

- The taxation of employer ETPs will be changed to reflect the removal of the RBL system and benefits tax.
- Greater use of tax file numbers will be encouraged.

EMPLOYER PAYMENTS (PAGE 41)

Currently, both superannuation benefits and employer ETPs are counted together in assessing if they exceed the RBL. As the RBL is to be removed for superannuation benefits, it is necessary to consider the taxation of employer ETPs, particularly the application of an upper limit on the amount of employer ETPs that receive concessional taxation treatment.

Employer ETPs will be comprised of two components — exempt and taxable. The exempt component will be any post-June 1994 invalidity amount and the pre-July 1983 amount. This will be exempt from tax. The taxable component will be the post-June 1983 amount. This will be taxed at 15 per cent for amounts up to $140,000 (indexed) for recipients aged 55 and over and at 30 per cent for those aged under 55. Amounts in excess of $140,000 will be taxed at the top marginal tax rate (plus Medicare levy). These arrangements will apply per termination and any payment must be made within one year of termination.

As superannuation benefits paid to those over age 60 will be tax free, employer ETPs will no longer be able to be rolled over into superannuation. This would have allowed people to put in place arrangements to avoid the intent of the caps on concessional and post-tax contributions.

TRANSITIONAL ARRANGEMENTS

Transitional arrangements will be put in place for individuals with employer ETPs specified in existing employment contracts as at 9 May 2006, provided payment is made prior to 1 July 2012. Under these arrangements, amounts will be taxed at 15 per cent up to $140,000 (30 per cent if under 55), 30 per cent up to $1 million and the top marginal rate plus Medicare levy for amounts over $1 million.

These employer ETPs can also be rolled into superannuation until 1 July 2012. However, any amounts above $1 million that are rolled over will have the excess above $1 million taxed at the top marginal tax rate plus Medicare levy. Amounts of less than $1 million will be treated as a taxable contribution to the fund but will not count against the $50,000 cap on concessional contributions.

Other employer payments

The taxation treatment of *bona fide* redundancy payments, approved early retirement scheme payments, or unused leave will not be changed.

NON-QUOTING OF TAX FILE NUMBERS (PAGE 43)

Tax on contributions

Currently there is no requirement for a person to quote their tax file number before making a contribution to a superannuation fund. However, a higher rate of tax is imposed on superannuation benefits if the member has not quoted their TFN.

The provision of TFNs with contributions being made to superannuation funds is important for the effective administration of the new superannuation system, particularly enforcing the superannuation contribution caps. Accordingly, where a TFN has not been quoted to a taxed fund, contributions will be taxed at the top marginal tax rate plus Medicare levy where taxable contributions to that fund for an existing member exceed $1,000 in a year. The $1,000 threshold will not apply for accounts opened on or after 1 July 2007.

Funds will not be required to apply the higher tax for accounts where a TFN has not been quoted until 30 June each year. This will give people until 30 June 2008 to quote their TFN if they have not already done so before the higher rate need apply. The additional tax will be refunded back to the fund where a valid TFN is provided within the period a fund can amend its own assessment (generally four years).

New arrangements will be put in place to minimise the number of accounts subject to the additional tax. Currently, when an employee completes a TFN declaration form for employment purposes they can also allow their employer to pass on their TFN to a superannuation fund. The provision of superannuation is an integral part of an employment package. Therefore, the legislation will be amended so that where an employee quotes a TFN for employment purposes it is automatically taken to be quoted for superannuation purposes. Generally, the employer must pass this onto a superannuation fund within 14 days of the TFN being quoted. Enforcement of this requirement will move from the Australian Prudential Regulation Authority to the ATO.

Where possible, the ATO will use its systems to match TFNs to members where non-quotation has occurred and contact members to organise for a TFN to be provided to their superannuation fund. The ATO will also undertake an education campaign to encourage members to provide their TFN to the fund.

Undeducted contributions

A superannuation fund will only be able to accept post-tax contributions for or on behalf of a member, if the member's tax file number has been quoted to the fund.

Benefit payments

Currently, where a person has not quoted their tax file number, the superannuation fund withholds tax at the top marginal tax rate on the payment of any pre-July 1983 component and post-June 1983 component.

Under the new arrangements, where a tax file number is not quoted only the post-June 1983 component (the taxable element) will be subject to withholding at the top marginal tax rate, as the pre-July 1983 component will be classed as an exempt component which is tax free.

UNTAXED SCHEMES

Key Points

- The taxation treatment for lump sum benefit payments from an untaxed source will be:
  - For those aged 60 or over — a rate of 15 per cent will apply to the total of all payments up to $1 million and the top marginal tax rate above that amount.
  - For those aged 55 to 59 — a rate of 15 per cent will apply for payments up to the low rate threshold ($140,000), 30 per cent above this amount up to the upper threshold ($1 million) and the top marginal tax rate above that amount.
  - For those aged under 55, a rate of 30 per cent will apply up to the upper threshold ($1 million) and the top marginal tax rate above this amount.
- Pension payments arising from an untaxed superannuation source to an individual over the age of 60 will be taxed at marginal tax rates with a 10 per cent offset. Payments to those below age 60 will be taxed at marginal tax rates without an offset (as is the case currently).

BENEFITS PAID TO INDIVIDUALS AGED 60 AND OVER (PAGE 47)

Lump sums

The post-June 1983 untaxed element of a benefit paid from an untaxed source will be taxed at 15 per cent up to $1 million and the top marginal tax rate above that amount. The $1 million will apply on a lifetime basis to each member of the fund. It will also be indexed to AWOTE and increase in amounts of $5,000.

Pensions

Pension payments will continue to be included in assessable income and taxed at marginal rates. However, pension payments (including where the pension commenced before 1 July 2007) will be eligible for a 10 per cent taxation offset. The return of contributions which are made towards the pension from the pensioner's own post-tax income and certain other amounts will be tax exempt once the person is aged 60 and above.

Certain pensions from an untaxed source do not include a pre-July 1983 component. This will continue under the new superannuation rules.

Reporting

Individuals will still be required to include lump sums and pensions in their tax return. Schemes will not need to report benefit payments to the ATO for RBL purposes for payments made after 30 June 2007.

PROPOSED ARRANGEMENTS FOR BENEFITS PAID TO INDIVIDUALS AGED UNDER 60 (PAGE 47)

Lump sums

For untaxed post-June 1983 elements paid to those aged 55 to 59, a rate of 15 per cent will apply for payments up to the low-rate ETP threshold ($140,000), a rate of 30 per cent above this amount up to $1 million and the top marginal tax rate above that amount. For those aged under 55, a rate of 30 per cent will apply up to $1 million and the top marginal tax rate above this amount.

Pensions

Pension payments will continue to be included in assessable income and taxed at marginal rates. Unlike payments for those aged 60 and over, they will not be eligible for the 10 per cent pension offset (until the recipient turns age 60).

Reporting

Individuals who receive benefit payments from untaxed schemes will be required to lodge a tax return and report these payments in the return as assessable income (as currently). Schemes will not need to report benefit payments to the ATO for RBL purposes for payments made after 30 June 2007.

Taxed benefits in untaxed schemes

Untaxed schemes can also pay benefits where tax has already been paid. This can include personal contributions and any earnings on those contributions and funded amounts which are taxed within the fund.

These benefits will be tax free if paid to a person aged 60 or over. The tax rules for taxed benefits for people aged less than 60 will also apply where relevant.

Death benefits

All lump sum death benefit payments will be tax free if paid to a dependant. For payments to non-dependants (irrespective of their age) the post-June 1983 untaxed element will be taxed at 30 per cent up to $1 million and the top marginal tax rate above that amount.

The taxation of death benefit payments as a reversionary pension will depend on the age of the primary and reversionary beneficiary. If the primary beneficiary was aged 60 or over on death, then payments to the reversionary beneficiary will be taxed at marginal tax rates less any deductible amount and less the 10 per cent offset (which will have been the tax treatment applying to the primary beneficiary before death). If the primary beneficiary was under age 60 at death, the pension will continue to be taxed at the reversionary beneficiary's marginal tax rate (less any deductible amount), unless, or until, the reversionary beneficiary is aged 60 or over, in which case the 10 per cent offset will apply.

A pension will not be able to revert to a non-dependant on death; rather, death benefit payments to non-dependants will have to be made as a lump sum.

ROLLOVERS TO TAXED SCHEMES (PAGE 49)

The transferring fund will withhold tax at the top marginal tax rate for amounts above $1 million. The first $1 million of the benefit to be transferred will be treated as a taxable contribution by the receiving fund. The remainder will form part of the exempt component in the receiving fund and not be taxed further.

MAKING IT EASIER TO FIND AND TRANSFER SUPERANNUATION

Key Points

- A new standardised form will be introduced to facilitate the transfer of benefits between funds. The maximum time period in which this transfer must occur will be reduced from 90 days to 30 days.
- The ATO will be more proactive in supporting the consolidation of lost member accounts.

NEW ARRANGEMENTS (PAGE 52)

Portability

Currently superannuation funds must transfer a benefit as soon as practicable after a request is received, and in any event within 90 days. The maximum time limit will be reduced from 90 days to 30 days. The 30 day period will commence after a person has provided all necessary information. Trustees will be required to follow up incomplete requests for transfers promptly.

All funds will be required to accept a standard form for portability requests. The form will include standard proof of identity requirements to ensure uniformity amongst funds. The standard form will make it easier for most members to provide the necessary information. The Government will consult on the development of this form.

Lost Members Register

The Government considers that there is scope to improve further the operation and effectiveness of the current lost member arrangements. The ATO will be given a more active role in facilitating the consolidation of lost accounts.

A phased approach will be put in place to reduce the number of people who are on the lost members register. This will include:

- rationalising existing processes to identify actual lost members including redefining lost members to exclude inactive accounts and more comprehensive reporting from funds;
- allow accounts of less than $200 to be paid tax free;
- an extensive letter campaign to lost members in 2007-08 and 2008-09 with lost account reviews to be conducted over a four year period through a combination of outbound phone calls and letters;

- establishing a web-based tool through which members can locate their lost accounts using their TFN and generate a pre-populated portability form; and

- by 2009-10, members will be able to electronically request consolidation of their accounts through the ATO website.

Regulation of self-managed superannuation funds

Key Points

- Additional resources will be provided to the ATO to better regulate self-managed superannuation funds.
- Streamlined reporting requirements with new administrative penalties for late returns and false statements.
- An increase in the supervisory levy from $45 to $150 per annum. This compares to the levy for small funds regulated by APRA of $500 per annum.

Improving the compliance of SMSFs

The growth of SMSFs has been increasing significantly over the past decade. The plan will make significant changes to the superannuation system. In particular, the removal of tax on end benefits will mean the restrictions on making contributions into superannuation will become critical to avoid abuse of the concessions given to superannuation. SMSFs currently account for approximately 50 per cent of contributions that are above the proposed contribution caps.

The Government is also concerned at the level of compliance by SMSFs with superannuation law and the level of trustee education and understanding of their responsibilities.

The Government will increase funding to the ATO to regulate SMSFs by $112 million over the forward estimates period. A range of changes are being made to ensure that SMSFs comply with their legislative obligations.

These changes will enhance compliance through increased ATO compliance activity, an increased focus on improving trustee awareness of their responsibilities, clearer auditor obligations and administrative penalties for late returns and false statements.

Changes to regulation of SMSFs

A single annual return will be introduced with the supervisory levy collected as part of the fund's income tax assessment. The form will consist of the annual regulatory return, the income tax return, and the member contribution statement. This will make managing an SMSF simpler and is estimated to save SMSFs approximately $80 per annum in compliance costs.

The ATO will also improve and strengthen the education and assistance available to help trustees of SMSFs through the use of information products, standard forms and other tools.

The reporting obligations for auditors will also be clarified to ensure independent auditors are properly informed of what they are required to report to the ATO.

In order to ensure lodgement of returns, and the accuracy of information reported to the ATO, new administrative penalties will be introduced for failure to lodge returns and for false or misleading statements to provide the ATO with greater flexibility in administering the law.

Fringe benefits tax will be removed from *in specie* employer contributions to superannuation funds. Contributions paid as money are not subject to fringe benefits tax and it is an anomaly that *in specie* contributions are currently treated differently.

SUPERVISORY LEVY

The Government has previously agreed that regulation of SMSFs should be broadly on a cost recovery basis. The current $45 levy has not changed since 1999 (when it was $200) and no longer adequately covers the reasonable costs of the ATO in regulating these funds. This compares to the levy for small funds regulated by APRA of $500 per annum.

From the 2007-08 financial year, the supervisory levy will be increased to $150 with the levy to be reviewed on a regular basis. The increase in the levy will enable the ATO to regulate this rapidly growing and diverse sector more effectively.

Fringe benefits tax will be removed from *in specie* employer contributions to superannuation funds.

Impact on fiscal balance ($b)

	2006-07	2007-08	2008-09	2009-10	Total*
Cost at 2006-07 Budget (excludes admin)		-1.6	-2.3	-2.3	-6.2
Parameter changes since 2006-07 Budget		-0.3	0.3	0.0	-0.1
Policy changes since 2006-07 Budget	-0.1	-0.1	-0.1	-0.1	-0.4
Administration costs	-0.1	-0.2	-0.1	-0.1	-0.5
Total cost of superannuation changes	**-0.1**	**-2.2**	**-2.3**	**-2.6**	**-7.2**
Less Provision made in 2006-07 Budget		-1.6	-2.3	-2.3	-6.2
Net budgetary impact of changes	**-0.1**	**-0.6**	**0.0**	**-0.3**	**-1.0**

* Figures may not sum to the total due to the effects of rounding