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The Treasury  
Langton Crescent  
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Dear Mr Lonsdale

### **A plan to simplify and streamline superannuation**

CPA Australia wishes to take the opportunity to provide further comment on the Government's plan to simplify and streamline superannuation.

Since our first submission of 9 June 2006, we have received numerous comments from our members and have further analysed the Plan. The attached submission builds on points raised in our initial submission, and raises new issues identified since. We make the following key suggestions, which we believe will reduce many of the complexities inherent in the proposed changes and provide a genuinely simplified superannuation system:

- the work test for contributions after age 65 be abolished with individuals able to contribute up to age 75 subject to the limits on concessional and undeducted contributions;
- excessive undeducted contributions are returned to the contributor, however, the earnings on the excessive contributions are not, nor are they taxed;
- the proceeds from the sale of a small business contributed to superannuation as an undeducted contribution be exempted from the contribution limits;
- the "10% rule" for determining the eligibility for deductibility of personal contributions be abolished to allow equal access to concessional treatment for all superannuants; and
- the proposed treatment of benefits paid from untaxed superannuation schemes be reconsidered to ensure parity in the treatment of members of these schemes compared to members of taxed superannuation funds.

Should you have any queries or require further information please contact CPA Australia's Superannuation Policy Adviser, Michael Davison, on 02 6267 8552 or by email at [michael.davison@cpaaustralia.com.au](mailto:michael.davison@cpaaustralia.com.au).

Yours sincerely

A handwritten signature in black ink, appearing to read 'GR', with a small dot above the 'i'.

**Geoff Rankin FCPA**  
Chief Executive Officer

cc M Davison



## CPA Australia

### Supplementary submission on a plan to simplify and streamline superannuation

#### Undeducted contributions cap and satisfying the work test

It is proposed that undeducted contributions be limited to \$150,000 each financial year with the 2005-06 limit applying to the period 10 May 2006 to 30 June 2006. There will also be provision for the annual limit to be averaged over a three year period, allowing a maximum contribution of \$450,000.

However, the *Post-tax contributions* fact sheet on the *simplersuper* website states that anyone taking advantage of the averaging provision will need to satisfy the contribution work test from age 65. In particular, anyone making a large contribution prior to age 65 will have to continue to satisfy the work test for the relevant years after they have turned 65.

This is a significant departure from the current situation, where the work test is applied at the time the contribution is made. We believe it will add considerable administrative complexity, particularly for superannuation funds, and will further disadvantage older contributors.

Individuals approaching 65 who utilise the averaging provisions in good faith that they will continue to satisfy the work test from age 65 will be unduly disadvantaged and have their retirement savings plans disrupted if they are no longer able to satisfy the work test on or after age 65, particularly in circumstances outside of their control such as retrenchment, forced retirement, ill health or death. We would also have the situation where an individual who has not had to satisfy any work test in the past or at the time of the contribution, may have to do so sometime in the future.

The abovementioned fact sheet does not provide full details of how the work test would be applied in relation to the averaging provision but we envisage there would be practical difficulties. In particular, how would an individual's contribution be treated in the first part of a new financial year when they are yet to have satisfied the work test for that year? Would they be able to retain the contribution in the fund on the proviso the work test will be satisfied later in the year. This would be a departure from the current application of the work test to individual contributions and would be creating additional complexity. If the work test were no longer satisfied, at what point would the contribution be refunded - at that time or at the beginning of the financial year - and what amount would be refunded - the whole contribution, the contribution for that year or a pro-rated amount?

The central tenet of the proposed changes is to simplify and streamline superannuation. However, the application of the work test from age 65 to the averaging provisions for the undeducted contribution cap would add considerable complexity.

Following on from the changes first announced by the Treasurer in February 2004, and built on in a *plan to simplify and streamline superannuation*, the work test for contributions after age 65 is the last remaining link between employment and superannuation. As mentioned in our previous submission, we believe there are significant benefits, in terms of simplicity and flexibility, in removing this work test. At the very least it should not be applied to the averaging provisions for the cap on undeducted contributions.

We suggest the work test for contributions between age 65 and 74 be abolished, allowing all Australians the flexibility to make contributions at any time before age 75. We also suggest it is appropriate that the current restrictions from age 75 continue.

As the limits for concessional and undeducted contributions are designed to ensure concessional tax treatment is targeted appropriately, we believe they are the only restrictions that should be applied to contributions. This would ensure simplicity and equity are maintained.

### **Refund of excessive undeducted contributions**

Following on from our previous submission, we believe that if excessive undeducted contributions are to be refunded, the earnings should only be taxed at the individual's marginal tax rate less 15% for the tax already paid on the earnings within the fund. This would be best achieved by the earnings being returned to the individual as income to be included in their total assessable income.

However, this approach still does not take into account the difficulties in determining which contributions are excessive and to be refunded and how the earnings will be calculated, particularly when there have been multiple contributions made on multiple dates and multiple investments are being held. Nor does it take into account the impact of negative investment earnings. With such administrative complexity, the cost of determining the earnings to be refunded and the appropriate tax to be paid may actually exceed the tax raised.

As an alternative, and in keeping with the spirit of greater simplicity, we suggest the requirement for the earnings on excessive contributions to be refunded and taxed is removed and instead any excessive contributions are simply refunded. While there may be some trade-off in the penalties for non-compliance and revenue, we believe the benefits of avoiding new complexity far outweigh anything else.

### **Exemptions from the contribution limits**

It is proposed there will be certain exemptions from the undeducted contribution limit. Particular mention is given to the CGT exempt component from the sale of a small business. However, this component only represents part of the sale proceeds that may have been contributed to superannuation, with the balance being contributed as undeducted contributions.

Given a small business owner's business is often their only retirement savings, we suggest all of the proceeds from the sale of a small business should be exempt from the undeducted contribution limit.

Following on from our previous submission, we also believe benefits transferred from overseas superannuation funds should be exempt from the contribution limits. Given these benefits are treated as if they have been accumulated in the Australian superannuation system, i.e. they are taxed accordingly, the individual should have the opportunity to add them to their Australian superannuation benefits. Applying the limits may actually make it difficult, if not impossible, for individuals to transfer their retirement savings into Australia as there will be situations where overseas funds will not permit partial transfers of benefits. As such, the transfer amount should be exempted from the limit on undeducted contributions and the amount elected to be treated as taxable contributions, ie the earnings, should be exempted from the concessional contribution limit.

We understand from discussions with Treasury officials there may be concerns that such an exemption may provide the opportunity for individuals to funnel contributions through overseas superannuation funds and hence bypass the contribution limits. However, we believe the risk of this is low, due to the difficulties involved with residency, termination of employment, taxation and payment rules, compared to the importance of allowing, and encouraging, expatriates to consolidate their retirement savings in Australia.

## **Deductible contributions**

Section 4.4.2 of the Plan discusses simplification of the rule to determine a person's eligibility to claim a deduction for personal superannuation contributions, however it doesn't mention whether the "10% rule" will continue to apply.

The requirement for less than 10% of income to be attributable to employment in order to be treated as self-employed, and hence eligible to claim a deduction, is an arbitrary one which penalises many people who are largely self-employed and have little access to other superannuation coverage.

In recent history the employment environment has changed considerably with employment arrangements becoming much more flexible and more people now employed under casual or contracting arrangements. Many people who consider themselves largely self-employed have found that they may have lost their eligibility to claim a deduction for their superannuation contributions after taking on what may have been relatively small consulting or contracting roles. There is often a double whammy affect in that these contracting roles will only pay SG contributions and there is no provision for the contractor to make voluntary or salary sacrifice contributions. The result is individuals in this situation may end up with minimal superannuation coverage since they do not have any more than SG coverage from their employment and are not able to claim a deduction for their own contributions.

These people are at a distinct disadvantage compared to people who are fulltime employees or fulltime self-employed. As such, we recommend the "10% rule" be abolished to provide greater incentive and flexibility to people who have to make their own superannuation provisions.

We recognise such a move would also allow employees to claim a deduction for their personal superannuation contributions. However, with full deductibility being given to personal contributions, there is now essentially no difference between the treatment of employer, salary sacrifice and personal deductible (i.e. self employed) contributions, is there any reason why they shouldn't?

The \$50,000 annual limit on concessional contributions would control the concessions available and there would be no benefit in exceeding the limit as excessive contributions would be taxed at the top marginal tax rate.

Importantly, allowing deductibility for personal contributions would benefit those employees whose employers limit or do not provide for salary sacrifice contributions and are at a distinct disadvantage compared to employees who do have access to salary sacrifice.

Abolishing the "10% rule" would create a level playing field where all superannuants would have the same access to concessional contributions and the same flexibility in deciding if their voluntary contributions should be made from before or after tax income. The limits on concessional and undeducted contributions would ensure everyone receives the same concessions and such a move would be another important step in ensuring equity and simplifying the superannuation system.

## **Employer ETPs**

It is proposed that the concessional tax treatment of employer ETPs, i.e. payments made by an employer on termination of employment, would be limited to \$140,000 of the taxed component. While not strictly an employer ETP, there may be some risk that the CGT exempt component paid by a company to an employee aged over 55 on the sale of the business may be caught up by the limit on employer ETPs. As such, we ask that the amending legislation is drafted appropriately to ensure the CGT exempt component is specifically excluded from the definition of employer ETP.

## **Untaxed schemes**

Following on from our previous submission, we wish to restate our concerns that the proposed treatment of benefits paid from untaxed schemes is inequitable compared to the treatment of benefits paid from taxed funds.

We believe that if significant benefits, such as removal of the RBLs and abolition of benefits tax over age 60, are being provided to members of taxed funds, equivalent benefits should also be provided to members of unfunded schemes. Parity should be maintained so that the only difference between taxed funds and untaxed schemes is a tax on benefit to compensate for the taxes foregone on contributions and earnings. The current differential between the two is generally 15%, and we believe this should be maintained going forward.

Apart from the obvious differences between the treatment of untaxed schemes and taxed schemes, there will also be a flow on effect that will further exacerbate the inequities. For example, pension income paid from an untaxed scheme will be assessable income (albeit with a modest rebate) while pension income from a taxed fund will not be assessed. The result may well be the recipient of an untaxed pension being pushed into a higher tax bracket and being further disadvantaged compared to their taxed fund equivalent. In addition to the risk of being pushed into a higher tax bracket, benefits paid from untaxed schemes will also be subject to the Medicare levy, while benefits paid from taxed funds will not.

We believe a more equitable way to treat benefits from untaxed schemes can be found. We would be happy to provide access to our resources and membership base in order to work with Treasury to develop a solution.