

A Plan to Simplify and Streamline Superannuation

Submission to Treasury



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1. Policy – Annual Capping Limit on Undeducted Contributions and Commencement Date

The Government has initiated a Modification Declaration stemming from the 2006-2007 Annual Budget limiting the amount of undeducted contributions that can be placed into superannuation in any given year. This initiative has obviously been put in place to balance out the abolition of the RBL system, however, there are arguments for either no limit or a higher limit to apply.

Commencement Date

There is also some concern in regards to the commencement date of the capping limit. Any current plans put in place to invest large amounts of funds as undeducted contributions have now been put into potential disarray. By delaying commencement for a year, this would allow the member to make arrangements necessary to either carry out the plan or devise a new plan.

Reporting

Superannuation funds report on an annual basis from 1 July and current systems have been established on this basis. Having to make new reports on contributions for a period part way through the year is likely to add additional cost to the fund for programming purposes.

Taxation on Excess Contribution earnings

The requirement to tax earnings at the highest marginal rate on excessive undeducted contributions raises compliance issues. Superannuation funds will be reliant on the ATO informing them of excessive contributions.

As superannuation funds are only required to report contributions once a year, the administrative process will therefore be delayed, raising more issues, such as, what happens if the member leaves the superannuation fund prior to the ATO determination?

We recommend that this “surcharge” tax be eliminated and earnings to be taxed at normal rates with the excessive contribution returned to the member.

No Limit

The compliance and software costs associated with this limit will need to be recouped from all superannuation members even though the rules will only affect

a relatively small percent of the fund membership. There is also some concern with the complexity of these rules in monitoring the contributions.

Superannuation has always been touted as a retirement planning tool, limiting the contributions into superannuation effectively limits future retirement proceeds. For younger members of superannuation, contributions made will be preserved for a relatively long period, therefore ensuring that the funds are being used for retirement purposes only.

Limit with Indexation

There has been no indication in the publications from Treasury that an indexation will apply to the capping limit on undeducted contributions.

Given inflation, wage movements and interest rates, it is imperative that any capping of contributions includes an indexation, as the value of \$150,000 will be completely different in 3 years time.

Indexing in line with AWOTE (following current calculations used for Age Based Limits) and rounding the final indexed figure would ensure an equitable increase each year.

An annual indexation of contributions should meet most members retirement needs especially if contributing over a period of time.

Higher Limit

Whilst capping the undeducted contributions is not unreasonable, it would appear unreasonable to disadvantage members who have had plans in place to make larger contributions to meet their retirement needs.

An alternative would be to impose a higher capping limit. There are general fears amongst older members that the ability to build an effective retirement benefit will disappear under the weight of capping. Some members also have had plans in place for a number of years, which provide for significant contributions to be made closer to retirement. Under the new rules, this is no longer possible.

Due to the abolition of the RBL system, capping undeducted contributions is not unreasonable. However compliance costs, averaging monitoring, system modification, additional tax calculations on investment earnings and refunding of overstated contributions will place a high additional cost on superannuation funds.

Also, with RBL's being abolished and deductible contributions being capped to the extent on how much concessional tax treatment they can receive in one year on 1 July 2007, it would seem logical to bring these changes inline together, allowing funds to put through one set of change to systems and product documentation instead of several.

2. A less confusing system would be more appropriate and the easiest way would be to increase the level of contributions allowed each year.

2. Policy – Age Base Limits and Deductions

Under current arrangements, employers and self-employed persons are entitled to claim deductions up to the Age Base Limit for contributions made on behalf of employees and for self-employed. The age base limits are indexed inline with AWOTE each year.

Under the proposal set out in the budget, the age base limits will be abolished with a set dollar figure of \$50,000 p.a. for each employee/self-employed person regardless of age (a transitional period allowing for \$100,000 for people over age 50 up to the year 2012 has also been proposed).

No mention of indexation on these figures has been made in the proposal paper.

We recommend that indexation, in line with general wage movement (AWOTE index) be automatically applied each year to these limits.

Years leading up to retirement generally provide higher levels of income and lower ongoing costs (education, housing, mortgages) as such the ability to provide for retirement is often improved.

Limiting the limit to \$50,000 restricts the capacity of many contributors to build up superannuation, which they were unable to do in previous years.

We therefore recommend that the \$100,000 transitional limit for persons over age 50 be retained and indexed annually in line with AWOTE.

Furthermore, whilst employers and self employed will be entitled to receive a deduction for the whole contribution (regardless of whether that figure is \$15,000 or \$150,000) the receiving superannuant will be charged tax on the excess over \$50,000 at the highest marginal tax rate.

We see this change as an extra compliance burden, not only for superannuation funds but also for the ATO. For example;

Joe Black is employed by ABC Plastics Pty Ltd and XYZ Sublime Limited; Joe has one amount of \$50,000 paid into his Fiducian superannuation account over the course of a year and another amount of \$40,000 paid into his AMP superannuation account.

How does the ATO determine, which contribution receives the 15% concessional tax treatment and which contribution pays the higher marginal tax rate?

Superannuation funds are only required to report contributions once a year. This administrative process will therefore be delayed, raising more issues, such as, what happens if the member leaves the superannuation fund prior to the ATO determination?

We recommend that this “surcharge” tax be eliminated and limit the deductions claimable by the employer and self-employed to the limits imposed.

3. Policy – Removal of Compulsory Withdrawal of Superannuation Funds at age 65

The proposal removes the compulsory withdrawal requirement at age 65 allowing members of a superannuation fund to hold their monies in superannuation indefinitely. This amendment takes affect from 9 May 2006.

Given the removal of compulsory withdrawals, increasing the age for contributing deductible contributions up to age 75 and the capping of undeducted contributions, we recommend increasing the allowable contribution age for all types of contributions to age 75 by removing the work test.

Removing the work test for contributions over age 65 will further simplify the current proposed system.

4. Policy – Superannuation Pensions

Clarification of new pension rules

The detailed outline states that the new rules will replace all existing 5 pension and 7 annuity rules however also states that the existing pensions will meet new minimum standards.

Clarification of whether the new existing rules will have an end date, such as from 30 June 2007, these products will no longer be able to be purchased however existing products will continue to be valid?

Further clarification of whether the minimum pension standards will be able to be applied to existing income streams is required.

Complying income stream products

Many pensioners purchased complying income stream products in order to access the higher Pension RBL. In exchange for this benefit, their capital is not accessible. Since the RBL system is being removed, surely it would be equitable to allow these pensioners to transfer their restrictive income streams to a new flexible pension product.

Three tier pension tax system

The proposed rules have created a 3-tier taxation system for pensions:

1. Up to age 55: Pension payments are taxed as assessable income.
2. Age 55 to 60: Pension payments are taxed as assessable income with a 15% rebate
3. Age 60+: Pension payments are not assessable income

Extend the 15% rebate

This goes against the grain of a simpler super system. Given the very tight limitations on accessing a superannuation pension before age 55 due to the condition of release rules, it would be reasonable to allow all superannuation pensioners under the age of 55 to receive the 15% tax offset. This would be simpler and more equitable.

5. Commencement of New Pensions

We are very concerned with the projected timeframe on passing legislation for the new changes. The current projected outcome does not allow superannuation funds an acceptable lead-time in developing and implementing new systems as well as producing new documentation such as Product Disclosure Statements (PDS) and/or supplements to the PDS.

6. Death benefits

Pension payments to non-dependants

There is no clear reason why a non-dependant (for tax purposes) should be unable to receive a death benefit as a pension. They are allowed to receive a lump sum benefit as they are an eligible beneficiary under the relevant SIS legislation. The most appropriate form for that benefit to take is best determined by the superannuation trustee.

We recommend that death benefits can be paid in the form of a pension to non-dependants at the discretion of the superannuation trustee.