



7 August 2006

General Manager  
Superannuation, Retirement and Savings Division  
The Treasury  
Langton Crescent  
PARKES ACT 2600

Dear Sir/madam

**A plan to simplify and streamline superannuation**

Please find enclosed our submission on the Government's plan to simplify and streamline superannuation. This submission is being made on behalf of Kingston Capital Limited (KCL) and represents the collective views of KCL management and KCL authorised representatives.

Although supportive of the Government's proposed plan, KCL believes a number of modifications could be made which if adopted, will not only assist clients to transition to the new superannuation regime, but will also facilitate further superannuation simplifications.

The enclosed submission seeks to focus on those areas most relevant to KCL and KCL clients and does not seek to provide comment on all aspects of the Government's proposed plan.

KCL appreciates the opportunity to make this submission and would be happy to provide further comments or submissions if need be. Please contact, KCL's General Manager, Superannuation Services, Peter Burgess on 08 8355 4744 should you wish to discuss any aspect of the enclosed submission in more detail.

Yours faithfully

A handwritten signature in dark ink, appearing to read "W. Killen", is written over the typed name.

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## Submission on the Government's plan to simplify and streamline superannuation

August 2006

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# **1. Introducing Kingston Capital Limited**

Kingston Capital Limited (KCL) is structured as a public company operating as an Australian Financial Services Licensee.

The company commenced operations in January 2001 in Western Australia with a small team of management and staff amongst the most experienced and respected in the industry, and with initial funds under advice of approximately \$250 million.

The company provides investment and financial planning advisory services to individuals, superannuation fund trustees, and charities. Individual portfolios are constructed based on specific risk profiles and client objectives. Currently funds under advice exceed \$800 million.

There are seven Advisers who own and operate their financial advisory practices as authorised representatives of KCL. Practices are located in Perth and Geraldton in Western Australia and Brisbane, Queensland. Each practice must meet ongoing compliance and performance standards in terms of KCL corporate policy.

KCL is a Principal Member of Financial Planning Association of Australia Limited and an Associate Member of the Association of Independently Owned Financial Planners.

KCL services are not advertised. Business growth is sourced from referrals from satisfied clients and investment performance.

Established in 2005, and located in Perth, Kingston Administration Services Pty Limited (KAS), is a wholly owned subsidiary company of KCL. Backed by highly experienced and qualified staff, KAS provides a comprehensive range of investment portfolio administration services for KCL clients, and superannuation administration services for KCL Self Managed Superannuation Fund clients.

# **2. Industry participation**

Historically, KCL has utilised a small APRA fund (SAF) structure to provide superannuation advice to clients and to compliment KCL's unique approach to investment management. Similar to a SMSF, a SAF is restricted to no more than four members and the trustee of the fund (which in the case of a SAF must be a financial corporation) is permitted to allow members to have direct input into the investment decisions of the fund without being restricted to a pre-determined list of investment options.

KCL currently provides superannuation advice to over 500 SAF clients with a combined asset value of over \$300m, and an average superannuation account balance of around \$700,000. In addition to providing investment advice to these clients, KCL also provides superannuation strategy advice incorporating superannuation tax minimisation strategies and retirement income strategies.

KCL also provides investment advice to a large number of SMSF clients and in recent times KCL has developed a SMSF administration service for SMSF trustees requiring an end-to-end SMSF administration solution.

### **3. Submission overview**

Overall, KCL is very supportive and applauds the objectives of the Government's proposed plan. However, KCL believes a number of modifications could be made which if adopted, will not only assist clients to transition to the new superannuation regime, but will also facilitate further superannuation simplifications.

In particular, KCL believes further changes are required to the proposed contribution capping rules to ensure these rules are implemented in the most equitable and efficient way, and which do not unduly impose on the Government's retirement income policy objective of assisting and encouraging people to achieve a higher standard of living in retirement.

To avoid any unintended strategy consequences, KCL also believes modifications are required to the proposed changes to the taxation of death benefits, and to facilitate the transition to the new superannuation regime, commutations should be permitted and not unduly penalised in situations where a pension has previously been commenced as part of a strategy to minimise excess benefits tax.

### **4. Issues and recommendations for consideration**

#### ***4.1 Contribution limits***

The proposed averaging arrangements for undeducted contributions require individuals to satisfy the contribution rules (work and age based tests) for all the subsequent years to which the averaging relates. Undeducted contributions accepted under the averaging arrangements would require the trustees to monitor the individual's compliance with the contribution rules for up to two financial years following the financial year in which the contribution was made. In the situation where the individual failed to satisfy the contribution rules for all subsequent years to which the averaging relates, the trustees would be obligated to refund contributions received in a financial year in which the contribution rules were not satisfied.

The rationale behind the proposed averaging arrangements is consistent with the current arrangement which only allows trustees to accept contributions if the contribution rules have been satisfied. However, the proposed practice of allowing the trustees to accept contributions in advance of satisfying the contribution rules, necessitates a change to the application of the contribution rules during the averaging period in order to avoid unnecessary complications and costs.

Although these changes may ultimately lead to individuals being permitted to contribute up to \$300,000 more to their superannuation under the averaging arrangements than would otherwise be permitted, the expected cost to the Government would be out weighted by the practical benefits of not requiring trustees to continually monitor an individual's compliance with the

contribution rules for up to two financial years following the financial year in which the contribution was made.

It could also be argued that imposing additional monitoring requirements on trustees and individuals at this time is not consistent with the Government's stated objective of simplifying superannuation arrangements for retirees and making it easier to understand.

### **Recommendation No. 1 – Contribution Averaging Arrangements**

To simplify and streamline the application of the contribution averaging arrangements, consideration should be given to only requiring individuals to have satisfied the contribution rules in the financial year in which the contribution is made. Individuals should not be required to satisfy the contribution rules in any subsequent financial year to which the averaging relates.

The detailed outline of the plan states that scope would be provided for exemption to the contribution limits. The Government has so far stated that the CGT exempt component from the sale of a small business would not be included in the contribution limit. Another scenario often faced by KCL clients, and which involves individuals acquiring lump sums "earmarked" for retirement, is the transfer of a superannuation benefit from an overseas fund.

Under current arrangements an individual can elect to transfer their overseas superannuation benefit to an Australian fund. The portion of their benefit which reflects earnings on their overseas benefit while they were an Australian resident is treated as a taxable contribution in the Australian fund and is therefore subject to the 15% tax on contributions.

Given that in most cases the amount being transferred will exceed the proposed annual contribution limits, it is likely that including such amounts in the contribution caps will severely restrict the transfer of overseas superannuation benefits to Australia. In some situations, individuals could transfer their overseas benefit to an Australian superannuation fund on a "drip feed" basis but this is likely to require extended and difficult administration arrangements with an overseas fund simply to avoid overly restrictive annual limits on such transfers in Australia. Again, it could be argued that imposing such annual limits on the transfer of an overseas benefit to an Australian superannuation funds is not consistent with the Government's stated objective of simplifying superannuation arrangements for retirees and making it easier to understand.

It could also be argued that although the transfer of an overseas benefit to an Australian superannuation fund is processed as a contribution (and generally subject to tax both in Australia and the overseas fund), in reality it simply reflects the rolling over of a superannuation benefit from one fund to another. As rolled over amounts are not included in the contribution cap, neither should amounts transferred from an overseas fund.

### **Recommendation No. 2 – Transfers from overseas superannuation funds**

To encourage and facilitate the transfer of overseas superannuation benefits to Australian Superannuation Funds, consideration should be given to excluding transfers from overseas superannuation funds from the contribution caps.

Compared to the current age based limits on deductible contributions, the proposed flat dollar \$50,000 limit, is likely to result in lower accumulated superannuation savings at retirement for

some individuals. Under the current arrangement, an individual is permitted to “step-up” the value of their deductible contributions as they approach retirement and their circumstances permit. Under the proposed plan, to achieve the same result, individuals would need to start making large deductible contributions earlier in life and which in most cases is unlikely to be possible or desirable 10 or more years out from retirement.

### **Recommendation No. 3 – Maximum deductible contribution limits**

To improve contribution flexibility in the years leading up to retirement, and to ensure the proposed plan does not unduly limit or discourage the accumulation of superannuation benefits, consideration should be given to increasing the proposed maximum deductible contribution limit from \$50,000 per annum to \$100,000 per annum for individuals over the age of 50. This could be achieved by extending the proposed transitional arrangements for deductible contributions indefinitely for individuals over the age of 50.

It is proposed that the maximum contribution limits for both deductible and undeducted contributions will be applied on flat dollar basis with no allowance for indexation. Although the introduction of flat dollar limits is a simple approach, to maintain the present value of these limits over time, there will no doubt be a need to increase these limits in line with wages growth and inflation. The current approach to indexing RBL limits and maximum deductible contribution limits appear to be well accepted by the industry and does not unduly complicate the retirement planning process.

### **Recommendation No. 4 – Indexation of contribution limits**

To ensure the contribution limits retain their present value and to facilitate a transparent and easy to understand approach, consideration should be given to increasing the contribution limits in line with annual increases in AWOTE.

## **4.2 Death Benefits**

Under the proposed plan the current tax treatment of death benefits will largely be retained but with simplified taxation components. However, with the removal of the tax of benefits for individuals over age 60, a number of anomalies may arise with the payment of superannuation death benefits after 1 July 2007.

The non-tax dependants of an individual, who dies after age 60, will in most cases incur a tax penalty if the deceased chose to retain their benefit in the superannuation environment up until the date of death. No such tax penalty would apply if the deceased who prior to death satisfied a condition of release and chose to transfer their benefit out of the superannuation environment prior to the date of death. A simple but perhaps frustrating solution to this issue would be for all individuals upon turning age 60, and who have satisfied a condition of release, to cash out their superannuation and re-contribute this amount as an undeducted contribution to avoid the payment of ETP tax on death.

A similar situation arises for the non-tax dependants of an individual who is under 60 and has satisfied a condition of release. Unlike an individual who dies over the age of 60, an individual who dies under the age of 60 does not in most cases have the opportunity to transfer an amount

tax free to their non-tax dependants prior to death. As a result the non-tax dependants effectively incur a tax penalty for the early death of the individual.

In addition, it is proposed that superannuation funds will be required to maintain ETP components for each member of the fund beyond age 60, despite this information being largely irrelevant after 1 July 2007. ETP components would not need to be maintained after 1 July 2007, if death benefits paid to non-tax dependants were exempt from ETP tax.

### **Recommendation No. 5 – Death Benefits**

To simplify the payment of superannuation death benefits and to avoid payment anomalies, subject to the requirements of the SIS Act and the fund's governing rules, all superannuation death benefits be exempt from tax, regardless of the recipient, or the age of the deceased.

## **4.3 Non-Commutable Pensions**

Under current arrangements, individuals are permitted to structure a pension in a way which provides access to the pension RBL. In return, these pensions impose significant restrictions on the availability of capital and the flexibility of pension payments.

From 1 July 2007, it is proposed that the RBL system will be abolished and a new simplified definition of a pension will be introduced. Therefore, clients who had commenced a non-commutable pension prior to 1 July 2007, will no longer be compensated for the inflexible and non-commutable nature of their pension, and without further legislative amendments, will also not be eligible to benefit from the proposed simplified pension rules.

The amendment of SIS Regulation 1.06 to ensure all pension types can be voluntarily commuted, will not only facilitate the transition to the new simplified pension regime, but will also enable individuals to retain a non-commutable pension should it be required for Centrelink purposes. Similarly, the removal or the amendment of SIS Regulation 1.06(2)(f), which has the potential to significantly complicate the commutation calculation of a defined benefit pension, will enable such pensions to be commuted in a timely and cost efficient manner.

### **Recommendation No. 6 – Non Commutable Pensions**

To simplify superannuation pension arrangements for retirees and to facilitate the transition to the new pension regime, consideration should be given to amending SIS Regulation 1.06 to enable the voluntary commutation of non-commutable pensions.