



The SMSF Professionals' Association of Australia Ltd

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8 August 2006

Mr John Lonsdale
General Manager
Superannuation, Retirement & Savings Division
The Treasury
Langton Crescent
PARKES ACT 2600

Via email: simplersuper@treasury.gov.au

Dear John,

SUBMISSION – “A Plan to simplify and streamline superannuation”

Please find enclosed a submission from the SMSF Professionals' Association of Australia Limited (SPAA) in response to “A Plan to simplify and streamline superannuation”.

SPAA appreciates the opportunity to provide comments and feedback from the association and its members in relation to the Government proposals announced in the 9 May 2006 Budget.

The submission has been prepared by SPAA and is being made available to Treasury and SPAA members on a confidential basis.

If you have any queries or require further discussion or dissemination of issues within the submission, please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in black ink, appearing to read "A. Slattery", is positioned below the "Yours sincerely," text.

Andrea Slattery
Chief Executive Officer
SPAA

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TREASURY SUBMISSION
August 2006

**“A Plan to Simplify and
Streamline Superannuation”**



Self-Managed Super Fund Professionals' Association of Australia Limited (‘SPAA’)

SUBMISSION ON THE GOVERNMENT’S “PLAN TO SIMPLIFY AND STREAMLINE SUPERANNUATION”.

PURPOSE OF SUBMISSION

SPAA is recognised as being the Self Managed Superannuation Fund (‘**SMSF**’) industries peak umbrella organisation for SMSF specialist advice within the SMSF Industry. As such SPAA represents advisors providing expert advice and services to a significant component of the Australian superannuation system with current SMSF numbers estimated at approximately 317,241 (entities), with total assets totalling approximately \$208.4 billion (or 23.01%), ranking SMSFs second only to Retail superannuation funds by assets in a superannuation pool totalling approximately \$905.4 billion as at March 2006¹.

SPAA believes that it is therefore imperative that after having sought comment from its Membership that it make a formal submission on the proposals.

SPAA members endorse the Government's proposal's for the simplification of the current superannuation system so as to provide simpler superannuation arrangements for retirees, improved incentives to participate in the system and greater flexibility in respect of the timing and draw-down of retirement savings in retirement.

SPAA supports the general thrust of the plan to simplify and streamline superannuation. It believes that in the absence of detail it cannot fully endorse or support the proposals, particularly when consideration needs to be given to the many practical administrative applications that will be effected by the introduction of the proposals.

SPAA is seeking to ensure the Government and Regulators to ensure that the integrity of the superannuation system is maintained, while looking forward to the introduction of legislation which we believe will ensure a better retirement for all Australians.

¹ Source APRA Quarterly Superannuation Performance Statistics March 2006 (issued 29 June 2006)

ABOUT SPAA

1. SPAA is the leading and peak professional association for all SMSF professional advisors within Australia, including but not limited to auditors, actuaries, tax agents, accountants, financial planners, lawyers, risk providers, administrators, barristers, educators and so on.
2. SPAA is an independent association which represents the needs of its members. The SPAA constitution is built around the 'association' being an umbrella association of "Professionals caring for Professionals". SPAA has developed and is currently maintaining professional standards for the SMSF advice industry. As such the association provides vital support, independent certification of education, dissemination of regulatory and other industry specific technical information to professional advisors seeking to ensure that their competency is at the very pinnacle of knowledge and skills. Through a stringent professional accreditation designation process, SPAA members are endorsed as 'SMSF Specialists' in their field regardless of their existing professional accreditation, qualifications or affiliations, after having proved their competency in SMSF advice.

Through this formal professional accreditation programme, SPAA aims to establish its members as the consumer's 'adviser of choice' when it comes to advice and services relating to SMSFs. The SPAA specialist accreditation designation is to be seen as a symbol of authority and expertise in what is a highly complex and specialised sub-industry within the financial services industry.

3. SPAA has as its objectives the following:
 - 3.1. Representation of SMSF professional advisors regardless of other affiliations;
 - 3.2. To constantly improve & develop educational standards;
 - 3.3. To liaise with Regulators to achieve industry best practice;
 - 3.4. To provide industry networking opportunities for professional SMSF advisors;
 - 3.5. The provision of 'Specialist Accreditation' and endorsement by the 'Peak Body' for advice in SMSF within the financial services industry. Endorsement and accreditation that is easily recognised within the SMSF consumer marketplace as a symbol of 'Quality Standards' providing consumer protection through self-regulation;
 - 3.6. Independence and an independent accreditation processes; and
 - 3.7. Complementary best practices for existing industry professionals.
4. Our national board is comprised of the following people:
 - 4.1. Mr. Peter Hogan SSA - Chairman (Colonial First State – Sydney)
 - 4.2. Mr. Peter Fry SSA - Vice Chair (Peter Fry & Associates - Melbourne)
 - 4.3. Mr. Graeme Colley SSA - (Super Concepts – Sydney)
 - 4.4. Mr. David Ruddiman SSA - (Professionals' Choice Wealth Management – Brisbane)
 - 4.5. Mr. Nick Aston SSA - (Brentnalls NSW - Sydney)
 - 4.6. Ms. Michelle Crosby SSA - (ComSuper – Canberra)
 - 4.7. Ms. Sharyn Long SSA - (Sharyn Long Chartered Accountants – Perth)
5. Our Chief Executive Officer is:
 - 5.1. Mrs. Andrea Slattery SSA - (Adelaide)

6. Importantly SPAA engages all industry participants in the raising of advisory standards within what is a critically important sub-industry within the superannuation services industry, supporting the future financial well-being of many hundreds of thousands of Australians. SPAA recognises the significance of establishing the highest possible industry standards, and ongoing professional development of all industry participants in the attainment of excellence, and to the future 'integrity' of the industry.
7. SPAA has as part of its objectives the role of working with the Regulators to provide a self regulatory role in the SMSF Industry. We intend to assist the Regulators in the development and maintenance of professional standards and integrity of the industry.

SUBMISSION

This submission provides comments in the same order as the chapters in the publication '**A Plan to Simplify and Streamline Superannuation**' detailed outline which was released on 9 May 2006.

1. Taxation of Benefit Payments

1.1 Removal of Reasonable Benefit Limits

SPAA supports the removal of the Reasonable Benefit Limits (RBLs) as they are a cumbersome recording system which was relevant only to a small minority of superannuation fund members and employees. The proposed system which will abolish RBLs for superannuation system payments yet tax employer payments in excess of a set amount at the top marginal rate on a year by year basis is supported on the basis of simplicity.

1.2 Removal of Tax on certain Pensions and Lump Sums for over 60s

The removal of tax on pensions and lump sums for most superannuation system payments for those over age 60 is also supported. SPAA believes that this will encourage superannuation benefits to stay within the system for a longer period to be used for retirement purposes.

One difficulty that arises for those older than age 60 is the payment of death benefits to non-dependants. Where a pension has been payable to a member on their death the amount payable to dependants and non-dependants may consist of an exempt and non-exempt component. While the benefit payable to a dependant will be tax free irrespective of the age of the dependant or the amount of the payment, the position is different with non-dependants. As non-dependants will be taxed on the lump sum they receive it may consist of an exempt or non-exempt component. Where a pension has been previously payable to the member then the fund will need to retain records relating to the purchase price of the pension and the remaining undeducted purchase price. The records will need to be retained for taxation and Centrelink purposes.

Another issue is the payment of reversionary pensions. In many cases a person may commence a pension and nominate a dependant as the reversionary. However, over time the dependant may become a non-dependant because of a number of factors. The requirement of the relevant pension contract may be to pay a reversionary pension, however, the Budget proposal is to require that all benefits be paid to a non-dependant as a lump sum. This issue needs to be considered. One way of solving the dependant/non-dependant issue is by having only a single definition of dependant for both SIS and income tax purposes. It is SPAA's opinion that the SIS definition be adopted for both.

SPAA considers that it should be confirmed that those who are currently in receipt of an excessive pension who are at least age 60 and are members of untaxed funds will receive the full rebate on any taxable pension they receive.

Clarification should be provided on the application of the proposed system to overseas pensions and lump sums which are taxable in Australia. It is considered that pensions paid from a taxed superannuation fund to anyone over age 60 should be tax free irrespective of the country of source.

1.3 Payment Arrangements for those under 60

SPAA supports the simplification of payments into two components, the exempt component and the taxable component. However, there are some reservations on the calculation of the pre July 83 component and its administration.

It is considered that any legislation should combine the exempt component into one fixed amount at the set time to ensure simplicity. This will ensure there only one amount is recognised as the exempt component at the particular time. Any future exempt amounts will then be added to the pre-determined single exempt amount. The taxable component is then the total of the amount standing to the credit of the member less the total of any exempt amount for the member.

It is considered that records be maintained by the fund to verify the exempt amount standing to the credit of the member's account at the relevant time. In addition, members should be notified of their pre July 83 component in the next member report to be sent. The relevant records should be maintained by the fund for a period consistent with the record keeping requirements in the *Superannuation Industry (Supervision) Act 1993* (SIS Act).

One concern with the proposal to crystallise the pre July 83 component at a particular time relates to those who are a member of a number of funds. In many cases it is possible for many of these members to amalgamate all their benefits so that the pre 83 component applies to the whole of their benefits. However, there are members of many funds who only have limited or no opportunities to amalgamate or transfer a benefit which has a pre July 83 component attaching to it. Some allowance should be made for these members so that all benefits acknowledge that they have the longest eligible service period possible to keep discrimination to a minimum.

Under the Budget proposals the crystallisation of the pre July 1983 component at a particular time will result in a number of inequities between employees and the self-employed. Under the rules a person who is an employee is able to use the longer of the period of fund membership and employment. However, self-employed people are only able to use the period of fund membership including other periods of service to which the benefit relates. In view of other changes in the proposals creating greater equity between employees and the self-employed it is suggested that for purposes of crystallisation of the pre July 1983 component that the period of self-employment be used to determine a self-employed person's eligible service period rather than the period of fund membership.

It is considered that the post June 83 component for those 55 and older should continue to be indexed to changes in Average Weekly Ordinary Time Earnings (AWOTE).

SPAA considers that it should be confirmed that those who are currently in receipt of an excessive pension, are under age 60 and are members of untaxed funds will receive the full rebate on any taxable pension that they receive.

1.4 Permanent Disability Benefits

The proposals do not indicate whether disability benefits paid as pensions and lump sums for those under 60 will continue to receive the same treatment as they do under the current system in relation to rebates and tax free portions. In addition, clarification is required on the treatment of disability benefits after a person reaches age 60.

Under the current rules for the taxation of eligible termination payments (ETPs) employees are granted further concessions if the benefit paid is as a disability ETP. This further concession is not available to self-employed persons who may be

permanently invalidated in similar, if not identical, circumstances. In view of other proposals within the plan to simplify superannuation which places employees and the self-employed on the same footing it would seem reasonable to treat disability benefits paid from superannuation on the same basis for taxation purposes irrespective of occupational status.

1.5 Temporary Residents Leaving Australia Permanently

SPAA supports the continued taxation treatment of the payment of superannuation benefits to temporary residents when they leave Australia permanently.

2. Payment Rules

SPAA supports the proposal to introduce one type of pension from 1 July 2007 which will be an account based pension with an annual minimum payment standard and a maximum payment standard only for transition to retirement pensions. It also supports the proposal to allow pensions which are currently available under the legislation to continue if required by the provider or pensioner.

There needs to be clarification on whether pensions that exist as at 1 July 2007, with or without commutation restrictions, will be permitted to be rolled over to the new style of pension. SPAA suggests that pensions which are unable to be commuted under the current rules or in terms of a relevant contract be permitted to be rolled over within a limited time, say within 5 years or by 30 June 2012. SPAA also requests that where pensions are wholly rolled over to commence the new style of pension that they continue to receive Centrelink asset test and income test concessions in the same way as the original pension.

A number of pensions which include pre 83 components have already commenced. Clarification should be provided on how the pre July 83 component is to be calculated in these cases.

The proposed rules for pensions that commence from 1 July 2007 will provide a minimum payment for most pensions with the exception of transition to retirement pension and certain grandfathered pensions. Would it be possible to clarify whether the existing pension valuation factors and relevant method of valuation will continue, or be updated as necessary.

2.1 Clarification of when a lump sum is a lump sum, when a pension is a pension and when a commutation is a commutation

In view of the flexibility of the new style of pension permitted from 1 July 2007 clarification needs to be provided on the procedure required at the commencement of the pension, when commuted and when it is rolled over back to accumulation phase. For example, where a person chooses to commence the pension with the minimum amount of pension, can any amount received above the minimum amount be treated as a commutation. Clarification of these aspects would assist for taxation purposes and Centrelink assets and income test purposes.

A definition of 'reversionary' should be provided for pensions. There are currently a number of different meanings within the superannuation industry of the use of the word. SPAA considers that 'reversionary' should be limited to dependants for SIS purposes of the pensioner and his or her estate.

SPAA considers that the payment factors for the new style of pension should be expressed as a percentage of the account balance and not a number which is used as the denominator in the calculation.

In view of the new style of pension being an account based pension guidance should be provided for funds on the valuation of fund assets at the time the pension commences and each time the amount of the pension is to be calculated.

SPAA supports the use of one definition of 'dependant' for *Superannuation Industry (Supervision) Act*, *Retirement Savings Account* and income tax purposes. The use of one definition will provide simplicity and consistency in the treatment of the payments for these purposes.

SPAA supports the abolition of the compulsory payment rules, with the exception of the compulsory payment of benefits on member's death, from 10 May 2006 in line with the time of the Budget announcement.

3. Contributions Rules

3.1 Caps on Deductible and Undeducted Contributions

It is considered that the caps placed on deducted and undeducted contributions do not correctly consider future demographic trends and the potential inability of many members of the community to pay debts as early in life as previous generations. The contribution thresholds that have been decided on seem to be skewed in favour of younger high income earners which constitutes an elite section of the population. The demographics for the generations due to retire in the next 20-40 years are quite different in relation to saving, spending, number of income earners in a home etc from those who are currently nearing retirement whose statistics were used for current cap proposals.

SPAA considers that the higher threshold of \$100,000 be set for those who are 40 or older. In addition, the impact of the higher threshold should be permitted for between 10 and 15 years to allow those who do not have sufficient superannuation to fund a reasonable amount in retirement. It is suggested that the higher threshold be set at the current level for those 50 and older (\$105,113) and indexed at AWOTE to maintain parity with changes in the value of money.

It is considered that a longer period than three years be used to determine the operation of the higher cap. SPAA suggests that a minimum of a 5 year cap be used to allow for the transfer of business property into a self-managed superannuation fund.

3.2 Capital Gains Tax Concessions and Undeducted Contributions

Under the current system taxable capital gains of up to \$500,000 earned on active assets over a person's life time can be exempted from tax if it is used for a person's retirement. While this is commendable, it does not take into account other small business people who intended to use other business assets as their superannuation and are unable to transfer the proceeds of those assets to the superannuation fund at or near the time of their retirement. It is considered therefore that any capital gains on the sale of business assets should be allowed to be transferred to a fund. However, the small business concession for retirement should continue to apply only to active assets.

3.3 Employer contributions, salary sacrifice contributions, or deductible contributions for the self employed

SPAA is of the opinion that the proposed introduction of a 'new' type of limit on the level of contributions that is taxed in the fund at a concessional rate creates undue complexity in administration. SPAA believes that it will be simpler from an administrative and reporting perspective to have all deductible contributions made within a year eligible for concessional tax at a rate of 15 per cent, regardless of the amount being contributed.

The administration of the contributions system by the Australian Taxation Office will mean that the reporting will occur after the end of the income year and that adjustments would need to be made to the relevant accounts. Any adjustment to the tax payable on contributions should be included in the year in which the excess

contributions are notified by the ATO. This would reduce the need to adjust previous accounts.

One issue that arises with excess contributions is the situation where a person has commenced an income stream with the excess contribution. Clarification should be provided on the procedure to be adopted with the commutation of the pension, for example, a transition to retirement pension and which components can be commuted to pay the tax on the excess deductible contribution or the income component on undeducted contributions.

SPAA is concerned that the reporting and collection of taxes on the excess contributions may result in a re-creation of the system that was in place for the superannuation and termination payments surcharge. Any system that is established should avoid any difficulties of that system so that assessments are completed within a prescribed period. Otherwise the huge delays in issuing assessments which became a feature of the surcharge system may be inherent in the proposed system.

SPAA supports the view that increased participation and eligibility to unlimited deductible contribution amounts for individuals by way of increased salary sacrifice or personal deductible contributions would have a profoundly downward effect on the dependency rates of many older Australians on government expenses, particularly in light of the ageing populations propensity to want to fund their retirement living and lifestyle commiserate with that being currently enjoyed.

3.4 Reporting of Deductible and Undeducted Contributions

Under the proposed system it would appear to be a requirement that contributions received by a fund for a year of income will need to be reported to the ATO. While this may present no difficulties where the contribution has been made by an employer there may be problems where contributions are made by an individual.

As an example, a self employed person who makes contributions to a superannuation fund is not required to make an election that the contributions, in whole or in part, constitute deductible contributions until an income tax assessment has been made by the Commissioner. The legislation also permits the Commissioner to accept late elections. If a fund accepts contributions and the individual has not made an election by the end of the financial year then the trustee is not able to accurately report whether the contributions are deductible or undeducted contributions.

Any legislation should provide clarity on how these contributions are to be treated for reporting purposes. Otherwise it may result in amounts being treated as taxable contributions or in other cases the co-contribution being paid on amounts that subsequently are notified as deductible contributions.

3.5 Member Undeducted Contributions

SPAA broadly supports the government's proposed capping of personal after tax contributions into superannuation. Concerns by SPAA over the reporting system to be used have been expressed in previous paragraphs. The issues relating to undeducted contributions relate to the co-contributions system, the period over which the periodic cap is applied and certain lump sum payments in excess of the cap.

In some situations a person may qualify for the co-contribution if undeducted contributions are made on a year by year basis and they satisfy other relevant criteria. With the introduction of the \$450,000 cap a person may be prohibited from making undeducted contributions in the subsequent two years. This would appear to prohibit them from qualifying for the co-contribution in those years, merely because they took advantage of the bring forward of the standard contribution amount. In other situations a member may make contributions in excess of the cap of which the whole amount could be refunded in the second and third years. Initially the excess

may qualify the person for the co-contribution, however, because of the refund of the undeducted contribution may result in the person not qualifying as the excess may not be counted as an undeducted contribution. These matters need to be clarified.

The current maximum cap is applied over a three year period which commences in the first year in which undeducted contributions exceed \$150,000. SPAA considers the three year period should be extended to a minimum of 5 years to enable large *in specie* transfers of property to be made to the fund. By extending the amount of the cap it will mean that some business real property, including farming property, can be transferred to the fund without unnecessary structuring via ungeared unit trust and ungeared company arrangements.

In certain cases in the past superannuation funds accepted large undeducted contributions which resulted from personal injury claims. Many of these were in excess of the proposed caps as they may relate to car accident victims or those who were severely personally injured as a result of an industrial accident. The superannuation fund was used as a useful tax concessional environment to pay pensions for the welfare of the injured person. It is considered that the cap should not be used to restrict the amount which is paid as a personal injury payment under relevant workplace and third party injury legislation.

3.6 Transfers from Overseas Superannuation Funds

SPAA considers that transfers from overseas superannuation schemes should not be included within the relevant caps. Under the operation of the ETP legislation the transfers can be divided into a taxable and non-taxable component. This results in the amount transferred being treated as an undeducted contribution or forming part of a post component. As some of the amounts transferred are in excess of the relevant caps and are, in effect, a rollover of benefits between superannuation funds then they should be excluded from the contributions cap.

3.7 Work Tests after age 65

SPAA welcomes the continuation of undeducted contributions and the extension of tax deductions for contributions made in respect of employees and unsupported persons up to the age of 75 providing the relevant work tests are met.

In relation to the work tests it is considered that a number of anomalies may arise for a person who is 63 or older and has made undeducted contributions in excess of the \$150,000 standard annual threshold but through some misfortune is unable to work during the relevant qualifying period. This could occur for example for a person who has contributed \$450,000 in one year and is injured or ill and is unable to work during the next two years. If the contribution rules are applied strictly then it will result in a refund of undeducted contributions plus the taxed earnings thereon

4. Self-Employed

SPAA supports the alignment of tax deductions for the self-employed and unsupported persons with those of employees. It also supports the extension of the co-contributions system to the self-employed.

SPAA considers the co-contributions system should be extended to anyone who makes undeducted contributions to superannuation, including those who are out of the workforce for periods of time to raise a family or are ill.

5. Untaxed Schemes

5.1 Level of the Pension Rebate

Most taxed superannuation funds do not pay income tax at the full rate of 15% due to fund expenses and the offset of other tax credits. Therefore any adjustment to the rebate provided for untaxed funds should take this into account

6. Other

6.1 Bankruptcy

Under the bankruptcy provisions the pension RBL is used as a threshold amount. Consideration needs to be given to an amount to replace the pension RBL threshold and to the definition issues between legislation.

6.2 Superannuation Guarantee

Under the Superannuation Guarantee legislation an employer may be exempted from contributing to superannuation where an employee has made an irrevocable election that they are in excess of their relevant RBL. This legislation should be amended to allow the election to be reversed so that future Superannuation Guarantee contributions can be made in respect of the member.

6.3 UK Pension Legislation

Under the UK pension legislation transfers of benefits can be made to a superannuation fund if the Australian fund has similar provisions to the UK system. The concern is that the transfer can only take place to a fund which is subject to taxation. Under the proposals a pension paid after age 60 will not be taxable. Clarification should be obtained to ensure that the transfer is able to take place and that the fact the payment of a pension after age 60 will not be taxable.

6.4 Transfer of Benefits Between Funds

The changes to the transfer of benefits are supported by SPAA, particularly the introduction of the standard form. This will allow any members to transfer without requiring them to answer unduly complex and in some instances unnecessary questions.

SPAA considers that where a fund is unable to comply with the time specified in the proposals that a penalty rate of interest should be imposed on the fund and added to the amount being transferred.

6.4 Indexation of Thresholds

SPAA considers that the various thresholds should be indexed to movements in AWOTE.

6.5 Amendment to Fund Trust Deeds

It is understood that in some cases various State governments will impose stamp duties on amendments to any trust deed that is required to be amended to meet the changed legislation. The various State and Territory Governments should be approached to ensure that there is no stamp duty imposed due to changes in the legislation.

6.6 Funeral Expenses

Under superannuation legislation, there is no specific provision for permitting payment of funeral expenses from a death benefit. In many cases a person who has paid funeral expenses is not, by reason only of that payment, a dependant. The SIS legislation should be permitted to pay funeral expenses.

FURTHER INFORMATION

We would be pleased to provide you with any further information in support of our submission.

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