



SELF-MANAGED INDEPENDENT SUPERANNUATION FUNDS ASSOCIATION

24 August 2020

The Honourable Michael Sukkar MP
The Treasury
Langton Crescent
PARKES ACT 2600

By email - prebudgetsubs@treasury.gov.au

Dear Sir

2020-21 pre-budget submission

The Self-managed Independent Superannuation Funds Association (**SISFA**) is Australia's original SMSF advocate, established in 1998 to represent the interests of trustees and industry to Government and the Regulators. SISFA's mission includes the encouragement of high professional standards through its professional membership and public education initiatives.

In these troubling times, SISFA believes there are number of measures that can be introduced by the Government that will reduce red tape and help stimulate economic activity. SISFA also believes there are number of bigger picture issues in the superannuation system that should be reviewed.

Consolidating thresholds

The superannuation system currently has a significant number of different thresholds for various measures, including:

- General transfer balance cap (\$1.6 million);¹
- Total superannuation balance (**TSB**) (varies depending on the measure);²
- Disregarded small fund assets (TSB > \$1.6 million);³
- Unused concessional cap carry forward (TSB < \$500,000);⁴
- Bring forward rule for non-concessional contributions (up to \$300,000 where TSB < \$1.4 million);⁵ and
- Extension of work test exemption (TSB < \$300,000).⁶

SISFA believes that many of these thresholds should be consolidated to a single threshold of \$1.6 million (indexed).

¹ Section 294-35(3) *Income Tax Assessment Act 1997* (Cth) (**ITAA 1997**)

² Section 307-230 *ITAA 1997*

³ Section 295-387 *ITAA 1997*

⁴ Section 291-20(3) *ITAA 1997*

⁵ Section 292-85(3) *ITAA 1997*

⁶ Regulation 7.04(1A) *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**SIS Regs**)

Consistency of indexation of thresholds

There is inconsistency in the superannuation system in how various thresholds are indexed, including:

- proportional indexation for personal transfer balance cap;⁷
- Indexation of general transfer balance cap to \$1.7 million on 1 July 2021, depending on CPI,⁸ and
- General concessional contributions cap of \$25,000 indexed in line with average weekly ordinary time earnings (**AWOTE**).⁹

SISFA believes that many of these thresholds should be indexed under the same formula tied to AWOTE. In particular, SISFA believes the proportionate indexation of the transfer balance cap should be replaced with flat indexation.

Abolish the work test

The work test¹⁰ currently discriminates against older members in society from making contributions. Given our aging society and longer life spans, SISFA believe this unfairly affects older members of our society. This is especially so given the caps on contributions (in particular that members with \$1.6 million of total super balance cannot make non-concessional contributions) which prevents excessive amounts being transferred into super for non-retirement reasons.

SISFA believes that the work test should be abolished.

Ability to convert market linked pensions into account based pensions

Super funds have been unable to commence market linked pensions since 2007. Market linked pensions commenced prior to that time have been grandfathered, cannot be commuted and must continue until the member dies.¹¹ Market linked pensions are now a legacy product that creates additional complexity and inflexibility to those members and super funds that continue to hold them.

SISFA believes that members in receipt of market linked pensions should have the option to convert them into account based pensions.

Non-arm's length income rules should be made proportionate

The non-arm's length income (**NALI**)¹² rules have been present in the superannuation system for many years. The consequences of triggering NALI are one the most serious in the tax system (ie automatic tax at 45% on NALI¹³ (this is a larger penalty than applies to Part IVA of the *Income Tax Assessment Act 1936*). Because of the serious consequences of their application, the administration of those laws has been on the basis that they were effectively treated as anti-avoidance provisions and only used for the most serious of cases.

It's the experience of SISFA's members that the administration of the NALI rules has been broadened in recent years. This has been brought into particular focus with the introduction of the non-arm's length expenditure rules and the ATO's release of Law Companion Ruling LCR 2019/D3.

Rather than NALI applying blanketly to all income tainted by non-arm's length dealings, SISFA believes that NALI should apply proportionately. Examples of that application include:

- If under non-arm's length dealings, a super fund acquires an asset for 10% below market value, then NALI should apply to 10% of the income and gains from that asset (ie not 100%);

⁷ Section 294-40 ITAA 1997

⁸ Sections 960-265, 960-280(1) and 960-285(7) ITAA 1997

⁹ Sections 291-20(2) and 960-285(7) ITAA 1997

¹⁰ Regulation 7.04(1) SIS Regs

¹¹ Regulation 1.06(8) SIS Regs

¹² Section 295-550 ITAA

¹³ Section 26(1)(b) *Income Tax Rates Act 1986* (Cth)

- If a related party of a super fund fails to charge an arm's length fee of \$10,000 in management fees for managing a super fund asset, then NALI should apply to \$10,000 (ie not all of the income and gains from that asset).

Remove the auto non-compliance for breaching section 17A and failing to be an Australian super fund

Under the current legislative settings, if a self managed superannuation fund (**SMSF**) breaches section 17A of the *Superannuation Industry (Supervision) Act 1993 (SIS Act)* or otherwise fails to satisfy the definition of an Australian Superannuation Fund the SMSF is automatically made non-compliant and is issued with a tax penalty that is equal to almost half the value of its assets. This is to be contrasted with other breaches of the SIS Act where the Australian Taxation Office (**ATO**) has a discretion as to whether to make the SMSF non-compliant.

SISFA believes the auto non-compliance for breaching section 17A, and failing to be an Australian superannuation fund, should be replaced with the ATO discretion that applies to other SIS Act breaches.

Fixes to the binding death benefit nomination system

SISFA believes the death benefit settings of the super system should be reviewed (see below). However, in the meantime, SISFA believes that changes should be made to the binding death benefit nomination (BDBN). These include:

- BDBNs should not lapse after 3 years¹⁴ – like a will, they should apply until they are revoked or replaced;
- “Informal” BDBNs should be allowed – like a will, if a BDBN does not meet the strict requirements, it should nonetheless be binding if it shows a clear intension to deal with super benefits.

Areas of the superannuation system that require review

SISFA believes there are a number of areas of the superannuation system that should be reviewed with a view of streamlining them and cutting red tape. They include:

- Tax settings - the taxation of superannuation is a complicated mess that has been amended in a piecemeal basis over many years.
- Death benefits – the death benefit system (including who it can be paid to and its tax settings) have hardly changed for decades. In SISFA's view it no longer meets the needs of modern society.
- Onshoring and offshoring issues - The interaction of the Australian superannuation system with foreign pension systems and the tax residency of Australian citizens is overly complex and no longer meets the needs of modern society.
- Superannuation guarantee – the super guarantee system is also overly complex and uncertain, in particular in its operation in relation to contractors.

If you have any questions in relation to this submission, please contact Phil Broderick on 03 9611 0163 or pbroderick@sladen.com.au

Yours Faithfully



Phil Broderick, Chair of Technical and Policy Committee

¹⁴ Regulation 6.17A(7)(a) SIS Regs

A handwritten signature in blue ink, appearing to read "C. Balalovski". The signature is fluid and cursive, with the first letter being a large capital 'C' and the last letter being a capital 'i'.

Chris Balalovski, Chair