The Association of Superannuation Funds of Australia Limited
ABN 29 002 786 290
ASFA Secretariat
PO Box 1485, Sydney NSW 2001
p: 02 9264 9300 (1800 812 798 outside Sydney)
f: 02 9264 8824
w: www.superannuation.asn.au

File Name: 2013/26

6 June 2013

Manager
Contributions and Accumulation Unit
Personal and Retirement Income Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: superannuation2013bill@treasury.gov.au

Dear Manager

RE: Income Tax Assessment and Other Legislation (Sustaining the Superannuation Contribution Concession) Amendment Regulation 2013; Superannuation Contributions

This submission from the Association of Superannuation Funds of Australia (ASFA) is in response to the request for comments on the proposed *Income Tax Assessment and Other Legislation (Sustaining the Superannuation Contribution Concession) Amendment Regulation 2013; Superannuation Contributions* (the "draft Regulations").

We note that the regulations are based loosely on those which operated under the superannuation contributions surcharge regime. We also note that this methodology is generally not in use as the contributions surcharge legislation does not apply with respect to contributions made on or after 1 July 2005.

ABOUT ASFA

ASFA is a non-profit, non-political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. We focus on the issues that affect the entire superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90% of the 12 million Australians with superannuation.

EXECUTIVE SUMMARY

In brief, ASFA is concerned that:

- The unanimous recommendation of the industry associations about the most appropriate methodology for determining defined benefit contributions – modelled on the calculation of Notional Taxable Contributions (NTC) - has been ignored.
- The regulations as drafted are deficient and their successful implementation will require the timely release of extensive interpretative material from the Australian Taxation Office (ATO) and a guidance note from the Actuaries Institute.
- The cost of implementation will be borne by all members of a defined benefit fund even though the Division 293 tax will be incurred by a limited number of members.
- Funds will be unable to meet their Member Contribution Statement (MCS) reporting deadline with respect to this information, potentially leading to general interest charge penalties on funds and those members subject to the additional 15% tax, unless remitted by the Tax Commissioner.

These and other matters are set out more fully below.

1. General comments

In the limited time available we have sought comments from our members. The consensus view is that the methodology chosen to determine the notional value of the contributions is not appropriate.

We have been unable to undertake a detailed examination of the effectiveness of the operation of the regulations, but initial advice from members with actuarial experience indicates that the regulations are deficient in a number of areas and will not achieve their intended purpose.

1.1. Methodology adopted

The draft Regulations are based, apparently somewhat loosely, on the regulations for determining the value of Notional Surchargeable Contributions under the superannuation contributions surcharge regime (the “surcharge”). The surcharge operated from the 1996-97 income year through to the 2004-05 income year (inclusive).

Currently, the only method being used for the determination of ‘notional’ contributions is that applied for the purpose of determining whether a member has excess concessional contributions under Division 292 of the *Income Tax Assessment Act 1997*.

In our submission on the exposure drafts of the *Tax Laws Amendment (Sustaining the Superannuation Contribution Concession) Bill 2013* (the “primary Bill”) and the *Superannuation (Sustaining the Superannuation Contribution Concession) Imposition Bill 2013*, we made strong representations that the methodology used for determining notional contributions with respect to defined benefit members be the same under both Division 292 and proposed Division 293. That is, the formula for determining the value of notional taxable contributions under Division 292 should be applied for Division 293 tax purposes.

The reasons for this are that:

- The method is known and understood by the industry; and
- It could be reasonably quickly implemented from a systems’ perspective, as generating the data generally would require only a relatively simple modification to ensure that programming which grandfathers the contributions cap is not applied for Division 293 tax purposes.

An additional concern with adopting the current methodology is the likely confusion it will create among members of defined benefit schemes. The use of different methodologies will result in the member being advised of two different amounts as the notional value of their contributions for the same period – one for excess contributions tax purposes and the other for Division 293 tax purposes. This will only compound the problem currently faced by these funds in explaining to members how the value of their notional contributions is determined. Quite simply, it would be inexplicable to a taxpayer why two different methods, resulting in two different valuations of defined benefit contributions, would be utilised by the ATO.

1.2 Cost of implementation

As stated above, the proposed valuation methodology is based on the surcharge. As such, it appears to be an approach that requires an individual calculation by an actuary of the value of accruing benefits on a member-by-member basis.

It is well recognised that a member-specific approach, while perhaps providing a more accurate and higher value, involves very complex calculations and is thus more costly.

In contrast, the approach currently adopted for valuing NTCs is category based, not member-specific. It is very much simpler and, importantly, it is already existing practice for the majority of defined benefit funds. Whilst we acknowledge that some funds are currently exempt from the requirement to calculate NTCs, adoption of a modified NTC calculation method is likely to be simpler and considerably less costly for them than implementation of the proposed surcharge-like method.

ASFA considers that to proceed with the current draft would mean very significant implementation costs for all defined benefit plans. We consider this to be an unnecessary cost given that the NTC method already exists.

The number of defined benefit interests left in Australian plans is dwindling rapidly. Of those, the number of members with incomes in excess of $300,000 would be a small minority. The draft Regulations appear to require member-by-member actuarial calculations for all defined benefit members even though only a tiny fraction of these will be subject to Division 293 tax. ASFA considers it unjustified to impose such a time-consuming and costly approach on all defined benefit plans having regard to the tax revenue likely to be raised.

> ***Recommendation 1***
> ***ASFA strongly recommends that, due to the complexity and cost of implementation and ongoing administration, the proposed method for determining defined benefit contributions not be proceeded with and instead be replaced by the current method for determining notional taxable contributions, with an adjustment to exclude the grandfathering provision.***

1.3 Deficiency of the regulations

ASFA has been advised that a cursory review of the regulations reveals significant deficiencies in their operation. The deficiencies arise both in their lack of clarity and in their achievement of the desired outcome.

A significant concern is that it would not be possible for an actuary to prepare the required reports without reference to extensive technical guidance by the ATO and a practice note by the Actuaries Institute. The need to refer to such extraneous material will increase the complexity and cost of the calculations, while the lead-time involved in their preparation will delay lodgement of the required information.

Recommendation 2
ASFA recommends that the Actuaries Institute be consulted on the difficulties of preparing the required calculations based on the regulations as currently drafted.

1.4 Meeting the reporting timeframe

The late release of these draft regulations, combined with the decision to choose a valuation methodology that is not currently in use, makes it unlikely that affected fund trustees will be able to provide the information in their 2012-13 MCS, which is due for lodgement by 31 October 2013. Trustees' options will be to either lodge the report late or lodge the report without the relevant information. Adopting either approach will expose the trustee to penalties for late or incomplete lodgement and will be costly and inefficient.

Where a fund member is subject to the new tax, the late lodgement will automatically expose the fund – and therefore, indirectly, all fund members - to the imposition of the General Interest Charge (GIC). Additionally, late lodgement of the MCS will delay the receipt of co-contributions and the Low Income Superannuation Contribution for members eligible for those benefits.

Recommendation 3
That the ATO hold discussions with industry to determine appropriate arrangements for the preparation and lodgement of the 2012-13 MCS

Recommendation 4
That the ATO hold urgent discussions with industry to determine appropriate administrative arrangements to avoid the automatic imposition of GIC that will be a direct result of the late advice of the valuation methodology to be used and the complexity associated with the methodology chosen.

2 Other related matters

2.1 Need for a new condition of release for payment of Division 293 tax out of a fund

We note that the current 'conditions of release' in Schedule 1A of the *Superannuation Industry (Supervision) Regulations 1994* permit a fund to release a member's benefits on receipt of a release authority issued under specified existing sections of the *Income Tax Assessment Act 1997*. Schedule 1 will need to be amended to include a new condition of release, allowing payment on receipt of a release authority issued under (proposed) section 135-10.

2.2 Difficulty meeting strict time requirements

The primary Bill provides that the Division 293 tax payable in respect of a defined benefit member is to be deferred to a debt account by the ATO, with payment of the 'debt account discharge liability' sought when an 'end benefit' becomes payable for the interest. This raises the potential for significant complexity, as it is not necessarily easy to identify when a benefit 'becomes payable'. ASFA considers that legislative time-limits for payment should only be imposed where the start time is clearly and unambiguously defined.

The calculation of the 'end benefit cap', being 15% of the employer financed component of the post 1 July 2012 accrual, is a similarly complex process and it is highly unlikely that funds could meet the requirement imposed under proposed subsection 134-65 to provide the information to the Commissioner of Taxation within 7 days of being requested to do so.

2.3. Legislative changes required for state based schemes

It would appear that each State jurisdiction may need to implement its own legislative changes to support this measure.

ASFA understands that some state based schemes currently have no capacity to accept a release authority for their untaxed accumulation scheme.

State based schemes may also need legislative amendments to facilitate application of the Division 293 tax to defined benefit members. It will not be possible to rely on existing provisions regarding application of the surcharge, as these recognise a surcharge debt as a liability against the fund/scheme and not, as required under the Division 293 tax regime, a liability against the member.

The need for these legislative changes may result in delays in the collection of Division 293 tax related amounts from members of state based schemes.

* * * *

I trust that the information contained in this submission is of value. We would be pleased to meet with you to discuss our submission.

If you have any queries or comments regarding the contents of our submission, please contact our principal policy adviser, Robert Hodge on (02) 8079 0806 or via e-mail to rhodge@superannuation.asn.au, or senior policy adviser Julia Stannard on (03) 9925 4027 or via e-mail to jstannard@superannuation.asn.au.

Yours sincerely

Fiona Galbraith
Director, Policy