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General Manager
Indirect Tax Division
The Treasury
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PARKES ACT 2600
Email: FinancialSupplies@treasury.gov.au

Dear General Manager,

EXPOSURE DRAFT REGULATIONS: GST FINANCIAL SUPPLY PROVISIONS

The Association of Superannuation Funds of Australia (ASFA) would like to provide this submission in response to the call for comments on the above exposure draft regulations and explanatory memorandum.

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 industry. 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.

General comments on the Measures

ASFA's particular interest is in those parts of the measures dealing with processing and assessing claims under life insurance policies, trustee and responsible entity services, and monitoring services.

Processing and assessing claims under life insurance policies

Whilst welcoming this change, which ASFA has previously sought, we note that it does not extend to funds with self-insured arrangements. ASFA requests that this be reviewed and either:

- Item 24(i) be amended to specifically cover self-insurance arrangements, or
- a statement be included in the explanatory memorandum to the effect that that entities with self-insured arrangements, as well as those with life insurance arrangements, may claim a reduced input tax credit (RITC) under benefit processing provisions (item 24(b)) with respect to the costs associated with processing and assessing of claims under such arrangements

Our strong view is that for the spirit of the change to be effectively enacted such that the regulations make it clear that a 75% RITC is available in respect of the acquisition of a service relating to the administration (setting up, maintaining, assessing claims and processing benefits) of life insurance arrangements (i.e. both self-insurance arrangements and life insurance policies)

it is essential that the Regulation 70-5.02 list of acquisitions that attract reduced input tax credits be expanded to specifically cover this matter and those activities.

Trustee and responsible entity services

ASFA notes that the operation of the rules around the acquiring of trustee services has been unclear since the inception of the GST regime. The government announced its intention to amend the rules in the 2010-11 Budget and over the past 18 months there has been extensive consultation with entities and sectors that may be affected by the proposed change.

ASFA's analysis of the change is that there will be some entities that gain and some that lose from the change. Overall ASFA supports the final decision to address the issue by reducing the RITC rate attributable to the acquisition by a recognised trust scheme of services from a trustee (other than those services explicitly exempted).

However, ASFA is concerned at the very short implementation timeframe and seeks a start date extension to 1 January 2013, but with the opportunity for an entity to elect to apply the amended rules from an earlier date should they desire to do so.

Monitoring services

ASFA supports the inclusion of new item 33 but questions why it has not been included in the item 32(b) list of items for which a 75% RITC is still available.

ASFA considers that this item is similar in operation and nature to item 24(h) except that the regulatory requirements to be met under AML/CTF are not specific to a single industry. Accordingly we request that item 33 be included in the item 32(b) list as an item for which a 75% RITC is still available.

Specific comments on the measures

Processing and assessing claims under life insurance policies

The need for a specific mention of this activity in item 24 of subregulation 70-5.02(2) highlights the difficulties that providers of financial supplies, and specifically superannuation fund trustees, have encountered in determining the scope of the existing RITC provisions. Item 24(b) permits an RITC with respect to the processing of applications, contributions, benefits and distributions. There has been some concern as to the exact scope of the term 'processing' and whether it extends to certain functions that are integral to the processing activity such as 'assessing' a person's entitlement to a benefit.

GSTR 2004/1 Goods and Services Tax – Reduced Credit Acquisitions sought to address the issue and considered the extent of operation of item 24(b) – processing of applications, contributions, benefits and distributions. It concluded, at paragraph 566, that:

Processing of *contributions, benefits and distributions* refers to the receiving and recording of member or client contributions to the fund or superannuation scheme. It also includes recording and disbursement by the manager, trustee, responsible entity, or the administrative service provider (on behalf of one of those entities) of benefits or distributions to the members, beneficiaries or investors.

However, at 543, in the context of bundled administration services, the ruling states that:

...if the administrative service includes elements not listed in item 24, these elements should be examined to determine whether they are ancillary, incidental or integral to one of the listed functions.'

Paragraph 544 then provides that:

Where a functional element that is not listed in items 24(a) to (h) is objectively viewed as ancillary, incidental or integral to a listed function or a group of listed functions, the acquisition is a composite acquisition of administrative functions. That acquisition is a reduced credit acquisition under item 24 (being a combination of the functions listed at items 24(a) to 24(h)).

With insured benefits, generally, superannuation funds only pay out in respect of an insured benefit when the claim is accepted by the insurer. In these cases, trustees do not assess claims. That function is performed by the life insurer. Where trustees may incur "assessment" costs is if they have concerns that the insurer has inappropriately rejected a claim. However it is questionable whether such costs incurred by the trustee are actually assessment costs under a life insurance policy.

Another circumstance where a trustee may incur "assessment" costs is if it is necessary to ascertain whether the member satisfies a condition of release. An insurance claim under a loss of limbs or an "own-occupation" definition in the insurance policy would be examples of where a trustee assessment might be required. However this is more in relation to paying the total benefit (of which the insurance payout is just one component) and it is again questionable whether this would be considered to be covered by proposed new item 24(i) - assessment costs under a life insurance policy.

There would also be some administration time/costs involved for the fund in dealing with the member and the insurer in relation to the insurance claim. ASFA would argue that these costs could attract an RITC under item 24(b) as this is part of, and integral to, dealing with the member's application for a benefit from the fund, of which claiming the insured benefit from the insurer is one component.

In other cases, the trust deed may specifically require the trustee to assess the claim. Where an insurance policy was in place the trustee would generally rely on the insurer to perform the assessment (at the insurer's cost). The trustee would then make its own determination after hearing the insurer's decision. ASFA considers that such assessments by the trustee are not assessments under a life insurance policy. Whilst the amendment will not pick these costs up we would argue that the activity is integral to the processing of the benefit and therefore there should be the capacity to claim an RITC under item 24(b).

Of particular concern to ASFA is that where trustees assess claims under self-insured arrangements, such as for death benefits, terminal medical conditions, TPD benefits, ill-health retirement and disability income, or undertake an assessment role under a life insurance policy, these costs would not be subject to an RITC unless they can be considered to be ancillary, incidental or integral to the processing of benefits.

Our strong view is that the spirit of the change is that a 75% RITC should be available in respect of the acquisition of a service relating to the administration (e.g. setting up, maintaining, assessing claims and processing benefits) of life insurance arrangements (i.e. both self-insurance arrangements and life insurance policies). ASFA considers that for this to be delivered it is essential that the Regulation 70-5.02 list of acquisitions that attract reduced input tax credits be expanded to specifically cover this matter and those activities.

To achieve this, ASFA strongly recommends that, in the first instance, proposed item 24(i) be amended to ensure that there is a 75% credit for the acquisitions of services relating to the **administration** of self-insurance and life insurance policies including the claiming of benefits under a life insurance policy. The provision should also extend to processing and assessing

claims in relation to death, terminal medical condition, permanent incapacity, temporary incapacity, ill-health, redundancy etc.

ASFA further requests that if there is any doubt that an RITC is not available under either item 24(b) or item 24(i) with respect to any of the following listed items then either item 24(b) or item 24(i) should be expanded to encompass them:

- the trustee's assessment of whether the member qualifies for an insurance payout
- the trustee's assessment of whether the member qualifies for a self-insurance payout
- the trustee's assessment of whether the member has satisfied a condition of release
- the trustee's assessment of whether the member qualifies for a particular benefit under the fund's governing rules

Trustee and responsible entity services

Implementation date

As indicated above, ASFA is very concerned at the short implementation timeframe and seeks a deferral of the commencement date to 1 January 2013. The changes have a significant impact on the GST treatment of superannuation funds and on GST administration systems. We have been advised that there will be difficulty in implementing the required changes by 1 July 2012.

Whilst the primary impact of the changes is on the GST position of superannuation funds, a significant indirect impact is on the GST accounting and processing function, much of which is done by external administrators and accountants. In many instances, the administrators and accountants will need to instruct the software providers to change external IT systems and/or change internal systems. While many IT systems may have the flexibility to change the RITC rate, few systems would have been designed to cater for multiple RITC rates.

This change also involves superannuation funds analysing all acquisitions that incur and instructing their administrators and custodians as to the appropriate treatment. While the first BAS may not need to be lodged until 21 August or 21 October in respect of quarterly lodgers the GST treatment of transactions processed from 1 July will need to be changed.

Of particular concern is that the reduction in the RITC rate for acquisitions of non-excluded services by a trustee will have a direct impact on the pricing of units in a unitised trust. Amended processes to address this issue would need to be in place by 1 July 2012 to ensure that the new tax situation is correctly reflected in the prices. ASFA sees difficulty in this being achieved by 1 July 2012, leaving trustees exposed to claims of unit pricing errors.

ASFA considers it would be very onerous for affected taxpayers to have to implement a stop gap measure to ensure the correct GST treatment of acquisitions between 1 July 2012 and the date on which the GST administration systems are able to be changed. As a consequence there is a high risk of failing to comply with the law during this transition period.

An added difficulty is the natural reluctance of businesses to commit to major systems changes until proposed legislative changes are actually in place. ASFA is concerned that by the time these regulations are made superannuation funds and their service providers will have less than two months to implement these changes.

Unbundling of services provided by, or acquired through, a trustee

On ASFA's reading of the exposure draft regulations, to the extent that a trustee provides services, or acquires services on the trusts behalf, which fall within one of the acquisitions in the proposed paragraph 32(b), the superannuation fund will be eligible to a 75% credit provided such services are separately identified on the GST invoice.

We note that some superannuation fund trustees currently provide administration services that would appear to be eligible for the 75% RITC. In particular we have seen a trend whereby as superannuation funds have become larger some of the services that were provided by external administrators are now being performed by trustees. But one example is the operation of call centres.

While we understand from our discussions with Treasury officials that the intent of the proposed regulations is that such services remain entitled to a 75% RITC, we are concerned that the diagram accompanying example 3 in the Explanatory Memorandum only deals with a bundled trustee service. That is, it does not contemplate that the trustee may 'unbundle its services so as to separately identify items for which the superannuation fund could be entitled to a 75% RITC, a 55% RITC or no RITC.

ASFA requests that examples of the unbundling of trustee services be included such that the operation of new item 32 may be more fully examined and explained in the context of both 'for profit' and 'not for profit' superannuation fund trusteeship arrangements.

If it is not intended that item 32 operate in such a manner then ASFA recommends that:

- the regulations be amended to clearly provide that trustee fees are entitled to a 75% credit to the extent that they relate to the items listed in sub-item 32(b)(i) to (vi), and
- the Explanatory Memorandum to the regulations be amended appropriately

It would also assist interpretation if the Explanatory Memorandum could provide some guidance as to how this unbundling could occur.

Recognised Trust Scheme

Many superannuation funds invest in special purpose trusts and companies. The superannuation fund commonly controls these entities and can own 100% of the units or shares. In many instances these trusts and companies are not managed investment schemes. In addition some of these trusts are grouped for GST purposes with the superannuation fund. Further, in some instances an entity acts as trustee for both the superannuation fund and the controlled entity. The overall net GST leakage will change depending on the extent to which the trustee charges one entity as opposed to the other.

ASFA is concerned that it may be administratively difficult if the proposed changes applied to a superannuation fund while an entity controlled or even wholly owned by it was taxed under the existing RITC regime.

ASFA recommends that amendments be made to allow a superannuation fund who controls an entity to apply the new regime to that entity.

Use of the term 'services'

ASFA understands that one of the intents of the change is that that a recognised trust scheme will be entitled to a 55% RITC on items except for goods. To achieve this, the proposed item 32 uses the word 'services' rather than 'supplies'.

In contrast with various overseas jurisdictions, "services" is not a defined term for Australian GST purposes. For example, in Canada the term "services" is defined to include "anything other than property". Such a definition makes the scope and application of the term "services" clear. The absence of a definition for "services" in Australia may result in a classification issue and some

uncertainty as to what the draft regulation applies to. For example, it may be difficult to determine whether some marketing or IT expenditure is a service or not.

One potential outcome is that the 55% RITC will not be available for expenses such as rent. This would create a bias to bundling such expenses into a trustee fee. Should this occur then the regulations would not achieve its objective.

ASFA recommends the term 'supply' be changed to, or defined as, 'supplies excluding the purchase of real property and goods'.

Item 7

We note that the proposed paragraph 32(b)(i) is limited to brokerage services covered by Regulation 70-5.02(2) Item 9. As it is not uncommon that a trustee facilitates the supply of a superannuation interest to a prospective member, ASFA recommends that this exclusion be widened to cover all acquisitions falling within Item 9.

The need for additional examples

ASFA also seeks examples that distinguish between the trustee acting in its own capacity and the trustee acting on behalf of the fund. This topic is hinted at by acquisitions D and E in the diagram above example 3. Our concern is that, although we have been advised that Treasury considers the regulations have been drafted in a manner which does not necessitate specific rules to cover these differences, the wording of Item 32 is such that a reader who has not been so informed by Treasury may struggle with determining the operation of Item 32 in certain circumstances.

To this extent we seek greater clarification through the inclusion in the explanatory memorandum of more and better examples.

ASFA suggests that the following examples be included and that the examples are based on a specific item (e.g. maintaining member and employer and trustee records and associated accounting) rather than the more generic "administration" service:

- A trustee, acting on behalf of the fund, outsources the member record services to a third party. The fund pays fees to the third party
- A trustee, acting on behalf of the fund, outsources the member record services to a third party. The trustee pays the fee and is reimbursed by the fund
- A trustee has contracted with the fund to provide member record services for a fee and in order to provide that service, outsources to a third party. The trustee charges the fund a specific fee for this service (i.e. the fee is not bundled with the fee/s for any other services). This fee may be different to the fee charged by the third party to the fund. Any difference (positive or negative) is retained by the trustee.
- A trustee has contracted with the fund to provide member record services for a fee. The trustee performs these services itself and invoices the fund for the fee as a separate unbundled item (the fee may also cover other administrative tasks such as processing of applications, contributions, benefits and distributions which are included in Item 24(a) to (g) and (i) of the regulations).
- A trustee has contracted with the fund to provide member record services for a fee. The trustee performs these services (as well as other trustee services) and invoices the fund on the basis of a bundled service. Can the trustee claim a 75% RITC on the member

record services component of the fee? If so, how does the fund determine the extent to which the 75% RITC is available?

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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, 0448 009 113 or via e-mail to rhodge@superannuation.asn.au.

Yours sincerely
Margaret Stewart



General Manager, Policy and Industry Practice