24 October 2014

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

By email: **ENCCTax@treasury.gov.au**

Dear Sir or Madam,

Reforming the Superannuation Excess Non–concessional Contributions Tax

Chartered Accountants Australia and New Zealand is made up of over 100,000 diverse, talented and financially astute professionals who utilise their skills every day to make a difference for businesses the world over.

Members of Chartered Accountants Australia and New Zealand and are known for professional integrity, principled judgement and financial discipline, and a forward-looking approach to business.

We focus on the education and lifelong learning of members, and engage in advocacy and thought leadership in areas that impact the economy and domestic and international capital markets.

We are represented on the Board of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

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Should you have any queries concerning the matters discussed in this submission, please contact Liz Westover via email at: **liz.westover@charteredaccountantsanz.com** or (02) 9290 5704.

Yours sincerely

Liz Westover FCA
Head of Superannuation

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Reforming the Superannuation Excess Non–concessional Contributions Tax

Chartered Accountants Australia and New Zealand is supportive of the Governments initiative to create a fairer outcome for Australians who contribute amounts to their superannuation in excess of their non-concessional contribution cap. Currently, many of those exceeding their caps have done so inadvertently and are subjected to excess contributions tax (ECT) at the highest marginal tax rate and in extreme cases, subjected to taxes of up to 93%.

Chartered Accountants Australia and New Zealand is supportive of a simple solution to rectifying the current ECT regime for excess non-concessional contributions. We are keen to ensure that these new measures are easy to understand and implement. However, we are mindful that even in keeping it simple, equity and integrity measures are required that will necessitate some level of detail.

Accordingly, we make the following comments on aspects of the draft legislation and accompanying explanatory memorandum (EM).

Associated Earnings

Actual earnings

While the draft legislation does not contemplate an ability of trustees to use an actual earnings rate rather than a deemed rate, Chartered Accountants Australia and New Zealand would like to reiterate our position that trustees should have discretion to use actual earnings instead of deemed earnings where they are able to clearly demonstrate and verify these amounts.

In some circumstances, the use of a deemed earnings rate could place an unreasonable assessment on a member. For example, where negative returns are made by the fund or where actual earnings are well below the deemed rate.

While the legislation seeks to give the relevant Minister the ability to declare a deemed rate, where such discretion is warranted, this will not apply where the circumstances leading to low or negative returns by a particular fund are not systemic in nature as was experienced during the Global Financial Crisis. An excess contribution for a member whose fund has suffered losses due to a bad investment will still result in potentially significant earnings needing to be declared, despite those earnings never having been realised.

We would encourage a review of this position to enable trustee discretion to use actual earnings.

Deemed rate of earnings

In the interests of simplicity, we are supportive of the use of a deemed rate of earnings. (notwithstanding our support of the ability for trustees to choose an alternative use of actual earnings). A deemed rate will provide an administratively simple solution for all superannuation trustees to deal with, particularly with the rate and amount to be calculated by the Australian Taxation Office (ATO) and provided to the fund for action.

Use of General Interest Charge

Chartered Accountants Australia and New Zealand are not supportive however of the use of the General Interest Charge (GIC) as the deemed rate. We believe this amount to be too high and does not reflect or proxy amounts likely to have been earned by the fund. While it may be seen as

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desirable to have a punitive aspect to this legislation, we believe the number of punitive aspects is too great and the deemed earnings rate is an easy means by which the overall and cumulative punitive measures can be eased (see commentary on the cumulative effects below).

We are supportive of a different measure being used, such as the Shortfall Interest Charge (SIC) as per Schedule 1, Section 280-105 of the Tax Administration Act 1953. SIC is currently calculated as the 90-day Bank Accepted Bill rate with a 3% uplift factor. GIC uses the same basis with a 7% uplift factor.

We agree it is appropriate to incorporate Minister's discretion to change the deemed rate from time to time where market conditions or other circumstances warrant such discretion being exercised. Such discretion would have been warranted, for example, during the Global Financial Crisis.

Start Date to calculate associated earnings

We support the use of a start date of 1 July in the year of contribution for calculation of associated earnings. This will be far easier administratively. The use of actual contribution dates will prove difficult where there are multiple contributions and in determining which contribution has caused the cap to be breached.

Excess non-concessional contributions determination and election

Refund of associated earnings

While the legislation is clear that an individual can elect to release or not release excess non-concessional contributions, it appears they can also elect whether or not to release the associated earnings. If the intention is for associated earnings to be refunded where sufficient funds are held by the fund to do so, then the legislation may need to specifically address this.

Section 96-1 states "You may elect to release…." in relation to excess concessional contributions, excess non-concessional contributions and associated earnings.

Section 96-7 also states that an individual may elect to release (or not) amounts under a determination. The definition of a determination for these purposes under Section 97-25 clearly includes associated earnings.

Furthermore, the EM talks about associated earnings being included in an individual's income tax return regardless of whether they were actually refunded. While we understand this to be the case where amounts are not available for refund (ie, a nil value in the fund), it is confusing as to whether earnings have to be refunded, were funds are available. Clarification in the legislation and an example in the EM would be helpful.

We agree that a choice of refunding excess amounts or not should be available to individuals, with ECT being imposed on available amounts that are not refunded, However, we believe that associated earnings need to be refunded as an integrity measure under these proposals. Otherwise, it will enable an individual to increase the amount they are able to hold in the superannuation environment, potentially outside the non-concessional contribution caps.

We would therefore encourage the inclusion of wording in the legislation to ensure that to the extent possible and where funds are available, associated earnings must be refunded out of the superannuation account. Consideration could also be given to including unrefunded earnings in the individual's future non-concessional contribution cap.

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Requirements for election

We would encourage the inclusion of wording in Section 96-7 (3) to enable an election to be made for a specific interest in a superannuation fund where multiple interests are held with one superannuation provider. This will enable members' interests to be better protected and provide clarity for the super providers. Section 96-12(1) would also need to be amended to reflect the election in the release authority.

Unsuccessful Release – making a further election

Amend wording in Section 96-7(5) that an individual 'must' make a further election rather than 'may' make a further election.

Release Authorities

Amend Section 96-12(1) to state that the Commissioner 'must' issue a release authority.

Consider changing 'and' to 'or' as an option between (a) and (b) for the Commissioner to issue a release authority. Option (b) will not be required unless (a) is unable to be complied with. Therefore, 'or' may be more appropriate wording.

Notifying Individual – unsuccessful release attempt

Section 96-40 (2) (b) needs to be removed – not applicable to excess non-concessional contributions as they are paid to the individual not the Commissioner. Should be replaced with the following (or words to this effect):

(a) receives………; and
(b) the superannuation provider has advised that they have been unable to release the full amount of the release authority.

Section 96-40 (3) will need to be amended to reflect that payment of amounts under a non-concessional contributions release authority are to the individual, not the Commissioner. However, the notice should still advise an individual how much has been reported to the Commissioner as having been paid to the individual.

Triggering of Bring Forward Provision

Chartered Accountants Australia and New Zealand are concerned that inadvertent triggering of the bring-forward provisions may exacerbate the impact of these reform measures. That is, a minor breach of the annual cap triggers the bring-forward provisions that results in a major breach in a subsequent year. These measures, although allowing for avoidance of an ECT assessment will still impact significantly on an individual because associated earnings will be calculated on the larger breach amount, not the minor amount that triggered the problem in the first instance.

Consideration should be given to allowing an individual to pursue a 'self assessment' determination from the Commissioner where they identify the problem, prior to the Commissioner issuing a determination under normal channels. Alternatively, when the Commissioner does issue a determination, the individual can make an election to refund the offending minor breach amount (and associated earnings). This would avoid the triggering of the bring-forward provisions and minimise the impact of a large associated earnings amount.

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Release of amounts from superannuation

Timing

Chartered Accountants Australia and New Zealand do not believe that a 7 day turnaround for payment of amounts under a release authority by super funds is sufficient, particularly when the 7 day period is calculated from the issue date of the release authority rather than receipt of the authority.

We believe a 14 day period would be sufficient to allow for postage delays as well as time to process and issue amounts to the individual member. We also support Commissioner's discretion being incorporated to extend this time where super funds are able to demonstrate an inability to comply with a 14 day time frame for a valid reason. We would anticipate a valid reason may include where fund assets need to be liquidated to enable payment to be made.

We would also encourage confirmation that where payments have not been effected within the 7 (or 14) day requirement, that it is still expected that the release authority be actioned, notwithstanding it is not within the required time frame. This issue has occurred in the past with other pieces of legislation (refund of contributions made to a fund that exceed the fund capped contribution limit). In this case, it was not clear as to what a super fund should do to comply with the law where the required time frames had lapsed.

Tax Components of refunded amounts

The draft legislation currently requires excess contributions amounts refunded plus associated earnings to first come from an individual's tax free component of their member account. We believe it is appropriate for the excess contribution to be refunded from the tax free component as that is how the contribution would have been treated by the fund. However, we do not believe the associated earnings should come from the same component. Rather, the associated earnings should come from the taxable component because this is how all earnings are treated in superannuation. This is another measure that on its own may be accepted as a punitive measure, however in conjunction with other measures can create an onerous outcome for the individual.

Double Taxation

Chartered Accountants Australia and New Zealand are concerned that the tax treatment of associated earnings refunded from a super fund has not been appropriately dealt with. In most cases, earnings within a super fund are currently taxed at up to 15%. Under the current proposals, these earnings (or a proxy amount under the deemed rate of earnings) are then also included in an individual's personal income tax return to be taxed at that persons marginal tax rate. This can and will result in double taxation of the earnings in most cases. This appears to operate in opposition to the intent of this legislation to return to a situation, as far as possible, that would have occurred if the excess contributions had not occurred in the first place.

One solution to this scenario would be to allow super funds to claim a tax deduction for any associated earnings refunded to the individual under these measures. The timing of the deduction would need to be confirmed (ie year of refund or year of contribution) to best correspond with the payment of tax by the fund. Other options may include a tax offset taken up by the individual to allow for tax already paid by the fund (where the member is still in accumulation phase).

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Cumulative effect of punitive measures

Chartered Accountants Australia and New Zealand have identified five layers of punitive measures associated with this legislation. While in isolation each of these may be identified as warranted on the basis of simplicity, cumulatively, they can have a significant impact on an individual that undermines the very reason for introducing this legislation in the first place. That is, to ease the financial burden and unfairness of the ECT tax, particularly in inadvertent cases of cap breaches.

The five measures are:

1) Start date of 1 July (or an alternative) for calculation of associated earnings, rather than using the actual date of contribution
2) Use of a ‘deemed’ rate of earnings rather than actual earnings of the fund, particularly in the absence of any choices around a method of calculation.
3) Use of the General Interest Charge (GIC) as the deemed rate of earnings. The GIC is particularly high compared with other potential earnings rates that could be used.
4) Double taxation – earnings within the super fund will have already been taxed within the fund and will then be further taxed at the individual’s marginal tax rate
5) Requirement that associated earnings be refunded out of a members tax free component instead of the taxable component, which may create a higher tax situation for the member and/or their beneficiaries.

We strongly encourage consideration as to where some or all of these measures can be alleviated. We have suggested some areas, in commentary above.

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