EXPOSURE DRAFT

treasury laws Amendment (2017 measures no. 2) bill 2017

EXPLANATORY MEMORANDUM

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1. Income tax relief for transfers within a fund to a MySuper product

## Outline of chapter

* 1. Schedule # to this exposure draft Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to provide asset roll‑over relief for mandatory transfers within a superannuation fund in the transition to a MySuper product.
	2. All legislative references in this explanatory memorandum are to the ITAA 1997 unless indicated otherwise.

## Context of amendments

* 1. MySuper products were introduced to improve the experience of superannuation members that accept the default option offered by their employer, by placing them in products that are appropriate and ensure their financial interests are protected.
	2. The transition to MySuper products must be completed by 1 July 2017.
	3. As a transfer of a default member’s account balance may create an income tax liability from the realisation of fund assets, asset roll‑over relief is currently available for such a transfer to a MySuper product in another superannuation fund to ensure that the default members are not disadvantaged.
	4. Schedule # to this exposure draft Bill will extend the asset roll‑over relief to mandatory transfers to a MySuper product within a superannuation fund. This will ensure that default members of superannuation funds will not incur adverse and unintended consequences when their account balances are transferred to a MySuper product within the fund.

## Summary of new law

* 1. Schedule # to this exposure draft Bill provides asset roll‑over relief to ensure default members of superannuation funds are not adversely affected if their superannuation benefits are mandatorily transferred to a MySuper product within the same superannuation fund.
	2. The roll‑over relief allows a complying superannuation fund to defer an income tax liability for assets transferred to the MySuper product so that the liability will not arise until an ultimate disposal of the asset.
	3. Where the superannuation fund invests in a life insurance company or a pooled superannuation trust (PST) to support its default members, the same relief is also provided to those entities.
	4. The relief is also available to the interposed entities that transfer the assets pursuant to the mandatory transfer.

Comparison of key features of new law and current law

|  |  |
| --- | --- |
| New law | Current law |
| A trustee of a complying superannuation fund, a life insurance company or a trustee of a PST can choose an asset roll‑over to defer income tax consequences from a mandatory transfer to a MySuper product in another superannuation fund or within the same superannuation fund. | A trustee of a complying superannuation fund, a life insurance company or a trustee of a PST can choose an asset roll‑over to defer income tax consequences from a mandatory transfer to a MySuper product in another superannuation fund. |
| A trustee of a trust, which is not a PST, can choose an asset roll‑over to defer income tax consequences from a mandatory transfer to a MySuper within the same superannuation fund. | No equivalent. |

## Detailed explanation of new law

* 1. The amendments ensure an asset roll‑over can be chosen by a transferring entity in relation to a transfer of a complying superannuation fund member’s accrued default amount to a MySuper product within the same superannuation fund, if certain conditions are satisfied. [Schedule #, items 2 and 6, section 311‑1 and subsection 311-12(1)]
	2. The transferring entity can be:
* a trustee of a complying superannuation fund;
* a life insurance company;
* a trustee of a PST; or
* a trustee of an interposed trust.

[Schedule #, item 6, subsection 311-12(1)]

* 1. In this regard, complying superannuation funds, life insurance companies and PSTs may invest assets attributable to default members’ account balances in interposed trusts by acquiring units in those trusts.
	2. In such cases, the transfer of accrued default amounts to a MySuper product would involve:
* the complying superannuation fund, the life insurance company or the PST redeeming units in the interposed trust;
* the complying superannuation fund, the life insurance company or the PST applying for units in another trust supporting the investments in respect of a MySuper product; and
* the assets of the interposed trust attributable to the accrued default amounts being transferred to the interposed trust supporting the MySuper product as consideration for the application for the units in the interposed trust supporting the MySuper product.
	1. The asset roll‑over is being extended to interposed trusts because the redemption and the transfer of assets between the interposed trusts are capital gains tax (CGT) events that may give rise to the realisation of capital gains or revenue gains.
	2. An asset roll‑over allows the transferring entity to defer income tax consequences pursuant to the transfer. This will ensure that the members are not adversely affected by the transfer of assets supporting their superannuation benefits.

### Conditions for asset roll‑over relief

* 1. For a transferring entity to access the asset roll‑over, it must satisfy four key conditions.

#### Condition one – entity’s assets must support interests in a fund

* 1. The transferring entity accessing the relief must either hold the default members’ account balances or be the entity whose assets support the default members’ account balances.
	2. If the transferring entity is a trustee of the complying superannuation fund holding the default members’ account balances, the condition is satisfied if, just before the arrangement was made, the fund held any assets that are not complying superannuation life insurance policies or units in a PST. [Schedule #, item 6, paragraph 311‑12(2)(a)]
	3. If the transferring entity is a life insurance company, the condition is satisfied if, just before the arrangement was made, a complying superannuation life insurance policy issued by the entity was held by a complying superannuation fund. [Schedule #, item 6, paragraph 311‑12(2)(b)]
	4. If the transferring entity is a PST, the condition is satisfied if, just before the arrangement was made, units in the PST were held by a complying superannuation fund. [Schedule #, item 6, paragraph 311‑12(c)]
	5. If the transferring entity is a trustee of an interposed trust that is not a PST, the condition is satisfied if, just before the arrangement was made, all the units in the trust were wholly owned (directly or indirectly) by:
* the trustee of a complying superannuation fund;
* a life insurance company that has issued a complying superannuation life insurance policy that, just before the arrangement was made, was held by a complying superannuation fund; or
* a trustee of a PST that has issued units that, just before the arrangement was made, were held by a complying superannuation fund.

[Schedule #, item 6, paragraph 311‑12(2)(d)]

#### Condition two – accrued default amount must be transferred

* 1. In order for the transferring entity to access asset roll‑over relief, an accrued default amount must be compulsorily transferred to a MySuper product offered by the same fund.
	2. The fund is required to make the transfer if it offers a MySuper product and its default members are eligible to hold the MySuper product (see paragraph 29SAA(1)(a) of the *Superannuation Industry (Supervision) Act 1993* (SIS Act)). [Schedule #, item 6, subsection 311‑12(3)]
	3. An accrued default amount is broadly the entire balance of a member’s account where an investment choice has not been exercised or if it is held in a default investment option of the fund.
	4. Accrued default amounts must be transferred to a MySuper product by 1 July 2017 (see subsection 29SAA(1) and section 388 of the SIS Act).

#### Condition three – investment structures of default product and MySuper product must be substantially the same

* 1. In order for the transferring entity to access asset roll‑over relief, the investment structure of the default product to which the accrued default amount is attributable must be substantially the same as the investment structure of the MySuper product that the amount is transferred to. [Schedule #, item 6, subsection 311‑12(4)]
	2. This condition requires the default product and the MySuper product to invest in the same type of entities. That is:
* if the accrued default amount was invested in a life insurance company — the fund must invest in a life insurance company to support its MySuper product;
* if the accrued default amount was invested in a PST — the fund must invest in a PST to support its MySuper product; or
* if the accrued default amount was invested directly by the fund — the fund must directly invest the transferred amounts to support its MySuper product without investing in a life insurance company or a PST.

Malama Super holds a complying superannuation life insurance policy issued by Life Co to support members investing in its default product. Life Co uses the premiums received for the life insurance policy to acquire various assets.

As a result of the MySuper reforms, Malama Super decides to offer a MySuper product and determines that all members investing in its default product are eligible to hold the MySuper product. Malama Super intends to acquire units in Rock Trust (a PST) using amounts in the MySuper product rather than acquire another life insurance policy.

On 19 September 2016, Malama Super transfers the accrued default amounts of its members to its MySuper product. It is agreed that Life Co will transfer the assets supporting the life insurance policy to Rock Trust as consideration for the redemption of the life insurance policy.

Life Co would not be eligible for an asset roll‑over for the assets transferred to Rock Trust, as the investment structure of the default product and the MySuper product are not substantially the same. Life Co would be subject to the income tax consequences for the transfer of those assets.

* 1. The condition does not require the number of entities involved in the chain of investment to be the same. In transitioning to a MySuper product, the fund may consider the number of entities through which it invests and rationalise the number of interposed entities.
	2. Although satisfying this condition does not require a MySuper product to replicate the investment structure of a default product, any difference between the investment structure of the default product and the MySuper product must be necessary to facilitate the mandatory transfer of accrued default amounts to the MySuper product. For example, the condition will be satisfied if the difference in investment structure is necessary for the product to satisfy the requirements to be a MySuper product under Part 2C of the SIS Act.

Aumakua Super holds units in Michelangelo Trust to support the members investing in its default product.

Michelangelo Trust holds units in Donatello Trust, which holds units in Raphael Trust. Raphael Trust indirectly holds a diversified portfolio of assets through Leonardo Trust. All those trusts are wholly owned and are not PSTs. Consequently, Leonardo Trust is indirectly wholly owned by Aumakua Super and the assets in the diversified portfolio are attributable to the accrued default amounts of Aumakua Super members.

As a result of the MySuper reforms, Aumakua Super decides to offer a MySuper product and determines that all members investing in its default product are eligible to hold the MySuper product.

In order to comply with the MySuper rules of ensuring a lower fee structure, Aumakua Super intends to acquire all units in Zen Trust. Zen Trust (which is not a PST) would hold a diversified portfolio of assets, to support the members investing in the MySuper product.

On 27 September 2016, Aumakua Super transfers the accrued default amounts of its members to its MySuper product. It is agreed that Leonardo Trust will transfer the assets attributable to the accrued default amounts to Zen Trust, as consideration for the redemption of its units by Raphael Trust prompted by Aumakua Super redeeming its units in Michelangelo Trust (which triggered a flow on effect on Donatello Trust and Raphael Trust).

Leonardo Trust can choose an asset roll‑over for the assets transferred to Zen Trust, as the investment structure of the default product and the MySuper product are substantially the same, despite the reduction in the number of interposed trusts in the structure.

* 1. Under the substantially the same investment structure condition, the proportion of investment in particular types of entities must remain substantially the same. That is, if a quarter of the accrued default amount was invested directly by the fund and the remaining portion is invested in a PST, to satisfy this condition a quarter of the amount transferred must be invested directly by the fund and the remaining amount must be invested in a PST.

#### Condition four – account balances must be transferred within certain time period

* 1. The accrued default amounts must have been transferred between 29 June 2015 and 1 July 2017. These dates are consistent with the Government’s announcement for the extension of the roll‑over relief to transfers within a fund and the deadline for the transfer of a default member’s accrued default amount to a MySuper product. [Schedule #, item 6, subsection 311-12(5)]

### Choosing the asset roll‑over

* 1. If a trustee of a complying superannuation fund, a life insurance company or a trustee of a trust meets the four key conditions outlined above, they may choose a CGT and revenue asset roll‑over for each asset that is transferred to entities supporting a MySuper product. [Schedule #, items 6 and 15, subsections 311‑12(1) and 311‑42(1)]
	2. The choice is evidenced by the manner in which the transferring entity completes its income tax return for the income year in which the accrued default amounts are transferred (see section 311‑60).

#### Assets eligible for an asset roll‑over

* 1. Where a trustee of a complying superannuation fund transfers assets to a MySuper product within the fund, it can choose a roll‑over for those assets that, just before the arrangement is made, are reasonably attributable to the accrued default amounts of its members. [Schedule #, item 15, paragraph 311‑42(2)(a)]
	2. Where the transferring entity accessing the relief is a life insurance company or a trustee of a PST, the assets must, just before the arrangement is made, be reasonably attributable to the accrued default amounts of the members and be reflected in the value of the fund’s interest in the life insurance policy or the units in the PST. [Schedule #, item 15, paragraphs 311‑42(2)(b) and (c)]
	3. Where a transferring entity accessing the relief is a trustee of an interposed trust that is not a PST, the assets must, just before the arrangement is made, be reasonably attributable to the accrued default amounts of the members and the units in the interposed trust must be wholly owned (directly or indirectly) by:
* a trustee of a complying superannuation fund that holds the accrued default amounts; or
* a life insurance company or a trustee of a PST in which the trustee of the complying superannuation fund invests the accrued default amounts to support its default members.

[Schedule #, items 6 and 15, paragraphs 311‑12(2)(d) and 311‑42(2)(d)]

* 1. After the transfer is complete, the asset becomes an asset of the receiving entity.
	2. For transfers of accrued default amounts to a MySuper product within the same complying superannuation fund, a receiving entity must be:
* a trustee of the complying superannuation fund;
* a life insurance company whose complying superannuation life insurance policy is being held by the complying superannuation fund just after the completion of the transfer;
* a trustee of a PST whose units are being held by the complying superannuation fund just after the completion of the transfer; or
* a trustee of a interposed trusts whose units are wholly owned (directly or indirectly) by one of the entities listed above just after the completion of the transfer.

[Schedule #, item 15, subsection 311‑42(3)]

#### Consequences of choosing asset roll‑over for CGT assets

* 1. Section 295‑85 makes the CGT regime the primary code for determining the tax consequences of the gains or losses generated on the realisation of certain assets owned by a complying superannuation fund or a PST. Section 320‑45 provides for the same rules to apply for the complying superannuation assets of life insurance companies.
	2. If the asset roll‑over is chosen by the transferring entity, it disregards any CGT consequences associated with the asset transfer. Also, the receiving entity is treated as having acquired the asset for the transferring entity’s cost base (and reduced cost base). This ensures that any CGT consequences are deferred until a later dealing with that asset by the receiving entity (see section 311‑45).

#### Consequences for choosing asset roll‑over for revenue assets

* 1. A revenue asset is an asset for which a profit or loss on disposal would be taken into account in calculating assessable income, other than a capital gains or capital loss, and that is not trading stock or a depreciating asset (see section 977‑50).
	2. For revenue assets subject to the asset roll‑over, the transferring entity is taken to have realised the asset for an amount that would result in it not making a profit or loss on that realisation. Furthermore, the receiving entity is taken to have acquired the revenue asset for that amount (see section 311‑50).
	3. This ensures that any income tax consequences are deferred until a later dealing with that asset by the receiving entity.

## Consequential amendments

* 1. This measure inserts provisions into Division 311, so that the Division governs tax relief for mandatory transfers of amounts to a MySuper product, regardless of whether the MySuper product is provided by another complying superannuation fund or the same fund.
	2. Consequential amendments are made to various provisions in the Division:
* to ensure that the provisions that are applicable to transfers within a fund do not continue to restrict their application to transfers to another fund;
* to delineate the provisions which apply to transfers to another fund and those that apply to transfers within the same fund; and
* to clarify the entity that makes the choice for tax relief and which provision the choice is made under.

[Schedule #, items 2 to 5, 7 to 14 and 16 to 18, sections 311‑1, 311‑5 and 311‑10, paragraph 311‑10(2)(c), section 311‑15, paragraph 311‑20(4)(b), sections 311‑40 and 311‑45, subsection 311‑50(1A) and section 311‑55]

* 1. Finally, although the ITAA 1997 contains references to ‘MySuper product’ the term is not defined in the ITAA 1997. This exposure draft Bill introduces the definition, which refers to the meaning of the term given in the SIS Act. Thus, the existing references to the term are amended to refer to the meaning as provided by the dictionary in the ITAA 1997. [Schedule #, items 1, 3, and 19, item 7 in the table in subsection 40‑340(1), section 311‑5 and subsection 995‑1(1) (definition of ‘MySuper product’)]

## Application and transitional provisions

* 1. The new law applies to mandatory transfers of members’ accrued default amounts occurring on or after 29 June 2015. [Schedule #, item 20]
	2. In this regard, the new law is beneficial to, and has been sought by, affected taxpayers as it provides roll‑over relief for income tax consequences that may result from a mandatory transfer of a default member’s account balance to a MySuper product within the same superannuation fund.

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