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TREASURY LAWS AMENDMENT (MISCELLANEOUS AMENDMENTS)  
BILL 2019 – EXPOSURE DRAFT

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EXPOSURE DRAFT EXPLANATORY MATERIALS



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# ***Glossary***

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The following abbreviations and acronyms are used throughout this explanatory memorandum.

<b><i>Abbreviation</i></b>	<b><i>Definition</i></b>
Commissioner	Commissioner of Taxation
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
TAA 1953	<i>Taxation Administration Act 1953</i>



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# **Chapter 1**

## **Miscellaneous superannuation amendments**

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### **Outline of chapter**

1.1 Part 1 of Schedule 1 to the Exposure Draft makes miscellaneous amendments to legislation relating to the tax treatment of superannuation to ensure that the legislation operates as originally intended.

1.2 These amendments are changes to support the implementation of the 2016-17 Fair and Sustainable Superannuation package that improved the flexibility, sustainability and integrity of superannuation tax concessions.

### **Context of amendments**

1.3 Miscellaneous amendments to Treasury portfolio legislation are periodically made to remove anomalies, correct unintended outcomes and to improve the quality of legislation within the Treasury portfolio.

1.4 The Assistant Treasurer, the Hon. Stuart Robert MP, announced these changes on 30 and 31 October 2018.

### **Summary of new law**

1.5 These miscellaneous amendments address minor technical implementation issues that relate to the *Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016*.

- 1.6 Namely, these technical changes will:
- correct an error in the way that a transfer balance debit is calculated for the purposes of the transfer balance cap when market linked pensions and annuities, and life expectancy pensions and annuities, that are capped defined benefit income streams are commuted; and
  - ensure the untaxed element of a lump sum superannuation death benefit derived under section 307-290 of the ITAA 1997 (in circumstances where a deduction has been claimed with respect to insurance) is not included in the assessable income of the receiving superannuation fund if the death benefit is rolled over by a dependant of the deceased.

## Detailed explanation of new law

### Debit value for certain capped defined benefit income streams

#### *Background*

1.7 Since 1 July 2017, there has been a limit on the total amount of superannuation that can be transferred into the retirement phase. This limit is referred to as the transfer balance cap, with the general transfer balance cap set at \$1.6 million for the 2017-18 financial year.

1.8 A person's transfer balance account is a record of the events that count towards their transfer balance cap.

1.9 A person's transfer balance is calculated as the sum of the person's transfer balance credits less their transfer balance debits. Transfer balance credits reflect the value of the interest that supports the person's superannuation income stream. A transfer balance debit arises for certain transfers out of the retirement phase, such as when a person commutes a superannuation income stream.

1.10 An individual who exceeds their transfer balance cap may commute part of their superannuation income stream to reduce their transfer balance below their cap. An individual may also decide to voluntarily commute their income stream, either in full or partially, for example, to change superannuation providers.

1.11 Currently, the calculations set out in Subdivision 294-D of the ITAA 1997 for determining the transfer balance debit that arises when a capped defined benefit income stream (as set out at items 3 to 7 of the table in subsection 294-130(1) of the ITAA 1997) is commuted do not operate as intended. There are issues where a relevant capped defined benefit income stream is fully commuted or is partially commuted.

***Full commutation***

1.12 For a commutation of a capped defined benefit income stream as set out in items 3 to 7 of the table in subsection 294-130(1) of the ITAA 1997, the transfer balance debit for a full commutation of the superannuation income stream is currently required to be calculated by reference to the first superannuation income stream benefit the individual is entitled to receive after the commutation occurs.

1.13 However, in the case of a full commutation the individual is not entitled to receive any further payments after the commutation occurs because the income stream has ceased, in which case the transfer debit will be nil. This is not the correct outcome and was not the original policy intent of the legislation.

***Partial commutation***

1.14 For a commutation of a capped defined benefit income stream as set out in items 3 to 7 of the table in subsection 294-130(1) of the ITAA 1997, the transfer balance debit for a partial commutation of the income stream is currently required to be calculated using the value of the pension payment the person is entitled to receive just before the partial commutation occurs and the amount of the pension payment that the person is entitled to receive just after the partial commutation (see paragraph 294-145(1)(b)).

1.15 However, the amount required to be paid for a market linked pension in a financial year is determined on 1 July of that year and is not adjusted to take into account any partial commutations that are made during the year.

1.16 This means that the amount derived by applying the formula in paragraph 294-145(1)(b) is zero and, hence, the transfer balance debit arising on the partial commutation is also nil.

1.17 These unintended outcomes create the potential for an individual to incorrectly exceed their transfer balance cap and may result in an amount needing to be commuted and a potential tax liability. This is not the correct outcome and was not the original policy intent of the legislation.

***Amendments***

1.18 Part 1 of Schedule 1 to the Exposure Draft replaces existing subsections 294-145(1) and (6) of the ITAA 1997 with new subsections (1A), (1B), (6) and (6A).

1.19 The new subsections provide that, in the case of a full commutation of a capped defined benefit income stream covered by items 3 to 7 of the table in subsection 294-130(1), the transfer balance debit is the debit value of the superannuation interest that supported the superannuation income stream just before the commutation takes place. *[Schedule 1, items 1 and 2, section 294-145 of the ITAA 1997]*

1.20 The debit value of the superannuation interest just before the full commutation is the amount of the original transfer balance credit in respect of the superannuation income stream less the sum of the following amounts:

- the amount of any transfer balance debits (other than a debit arising under item 4 of the table in subsection 294-80(1)) in respect of the income stream before the commutation;
- the total amount of superannuation income stream benefits the person was entitled to receive before the start of the financial year in which the commutation takes place; and
- the greater of:
  - the sum of the superannuation income stream benefits paid during the financial year in which the commutation takes place; or
  - the minimum amount required to be paid under regulation 1.07B, 1.07C of the *Superannuation Industry (Supervision) Regulations 1994* or regulation 1.08 of the *Retirement Savings Account Regulations 1997* during the financial year in which the commutation takes.

*[Schedule 1, item 1, subsection 294-145(1) of the ITAA 1997]*

### **Example 1.1: Full commutation of a market linked pension**

Daniel was the recipient of a market linked pension (MLP1) on 1 July 2017 and this was the only superannuation income stream he was receiving. The transfer balance credit that arose in his transfer balance account on 1 July 2017 was \$1,829,697 (being the special value of his market linked pension at that time).

In the 2017–18 income year, Daniel received superannuation income stream benefits from the pension totalling \$91,485. In the 2018-19 income year, he received superannuation income stream benefits from the pension totalling \$91,941. The account balance of MLP1 as at 30 June 2019 is \$1,218,994.

As at 30 June 2019, no transfer balance debits have arisen in Daniel's transfer balance account in respect of his market linked pension.

Daniel fully commutes MLP1 on 30 June 2019. The debit that arises from this commutation is calculated as:

- the original transfer balance credit in respect of the pension (\$1,829,697); less
- the amount of any transfer balance debits that have arisen in respect of the pension (nil); less
- the total amount of superannuation income stream benefits Daniel was entitled to receive before the start of the 2018–19 financial year (\$91,485); less
- the greater of the superannuation income stream benefits Daniel has received in the 2018–19 financial year, and the minimum amount required to be paid to him under the regulations (\$91,941).

Therefore, the debit that arises in Daniel’s transfer balance account as a result of the commutation is \$1,646,271.

Due to the regulatory restrictions associated with market linked pensions, after the commutation, Daniel is required to commence a new market linked pension. As the new market linked pension (MLP2) is not a capped defined benefit income stream, the transfer balance credit that arises reflects its opening account balance of \$1,218,994. Following this credit, Daniel’s transfer balance is \$1,402,420. This figure is calculated as the net balance of Daniel’s transfer balance account after the following amounts have been accounted for:

- the original credit for MLP1; less
- the debit for MLP1; plus
- the new credit for MLP2.

That is  $\$1,829,697 - \$1,646,271 + \$1,218,994 = \$1,402,420$ .

1.21 The amendments made by the Exposure Draft also provide that, in the case of a partial commutation of a capped defined benefit income stream that is covered by items 3 to 7 of the table in subsection 294-130(1), the transfer balance debit is the lesser of:

- the debit value that would arise if the commutation was a full commutation; and
- the amount of the superannuation lump sum that results from the partial commutation.

*[Schedule 1, item 1, subsections 294-145(1) and (2) of the ITAA 1997]*

1.22 The existing method for calculating the transfer balance debit for a partial commutation of a capped defined benefit income stream referred to in items 1 and 2 of the table in subsection 294-130(1) has not changed.

### **Example 1.2: Partial commutation of a market linked pension**

Lani was the recipient of a market linked pension on 1 July 2017 and this was the only superannuation income stream she was receiving. The transfer balance credit that arose in her transfer balance account on 1 July 2017 was \$1,863,050 (being, the special value of her market linked pension at that time).

On 30 September 2019, as part of finalising her divorce, Lani is required to transfer \$500,000 of her superannuation to her ex-husband. Lani partially commutes her market linked pension by \$500,000 and transfers it to her ex-husband's superannuation fund.

The transfer balance debit that arises in Lani's transfer balance account as a result of the partial commutation on 30 September 2019 is the lesser of:

- the debit that would arise if there was a full commutation; and
- the amount of the superannuation lump sum that is paid as a result of the partial commutation.

If the market linked pension were fully commuted, a debit would arise of \$1,548,600 (applying the calculation method for full commutations described in Example 1.1).

Therefore, the debit that arises in Lani's transfer balance account as a result of the partial commutation is \$500,000 (the lesser of \$1,548,600 and \$500,000). After the partial commutation, the balance in her transfer balance account is \$1,363,050.

## **Death benefit rollovers**

1.23 The *Treasury Laws Amendment (Fair and Sustainable Superannuation) Act 2016* amended the ITAA 1997 to include superannuation death benefits in the definition of 'roll over superannuation benefits'.

1.24 This has meant that, since 1 July 2017, a death benefit that is rolled over by a dependant will receive a taxation treatment that is consistent with that of member benefits that are rolled over. Namely, the rolled over benefit will not be treated as a superannuation contribution and will be non-assessable non-exempt income.

1.25 This amendment was intended to provide flexibility for dependants and allow them to rollover lump sums to a fund of their choice.

1.26 However, an unintended tax consequence arises where the superannuation lump sum death benefit that is rolled over comprises an untaxed element created by the application of section 307-290 of the ITAA 1997. Section 307-290 applies to create an untaxed element in a superannuation lump sum death benefit in certain circumstances where the fund has claimed deductions for insurance and self-insurance in relation to the death benefit.

1.27 Currently, where the lump sum death benefit is paid directly from the fund to a dependant, the benefit will be tax free in the dependant's hands because of section 302-60 of the ITAA 1997 (notwithstanding that section 307-290 may apply to create an untaxed element). Equally, if a deceased's benefits in the fund are used instead to pay a superannuation income stream to a dependant from the fund, section 307-290 does not apply.

1.28 However, if instead the lump sum death benefit is rolled over by the dependant to a different fund (Fund 2) the untaxed element created by the application of section 307-290 will be included in the assessable income of Fund 2 under item 2 of the table in subsection 295-190(1) of the ITAA 1997.

1.29 This has the consequence of reducing the amount of the gross benefit originally available to commence an income stream for the dependant from Fund 2 by the amount of the tax paid on the untaxed element. This treatment is unintended and may operate to penalise individuals that exercise choice and change funds.

1.30 The Exposure Draft amends the ITAA 1997 to exclude an amount that is an element untaxed in the fund. This is done by amending table item 2 in paragraph 295-190(1) to exclude an amount that is an element untaxed in the fund created by the application of subsection 307-290(4) of the ITAA 1997. *[Schedule 1, item 3, subsection 295-190(1) of the ITAA 1997]*

## **Application and transitional provisions**

1.31 The amendments commence on 1 July 2017 and apply from that date. *[Item 2 of the table in subclause 2(1) of the Exposure Draft and Schedule 1, item 4]*

1.32 The amendments will apply retrospectively because it was always intended that the legislation would work in this way.



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## **Chapter 2**

# ***Miscellaneous running balance account amendments***

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### **Outline of chapter**

2.1 Part 2 of Schedule 1 to the Exposure Draft makes amendments to the TAA 1953 that facilitate the Commissioner accounting for more tax debts in running balance accounts.

2.2 These amendments are part of the Government's commitment to the care and maintenance of Treasury portfolio legislation.

### **Context of amendments**

2.3 The Commissioner has established a number of running balance accounts to account for tax debts. Most commonly, running balance accounts are established for tax debts notified on business activity statements, as well as associated payments and credits. The current law creates technical difficulties that prevent certain tax debts from being accounted for in a running balance account. For example, the Commissioner has not established a running balance account for income tax debts.

### **Summary of new law**

2.4 Part 2 of Schedule 1 to the Exposure Draft makes amendments to the TAA 1953 that facilitate the Commissioner accounting for more tax debts in running balance accounts. This aligns the accounting treatment for the most common tax debts, such as income tax and business activity statement amounts, for taxpayers and the ATO. In addition, the same rules governing accounts and evidence of tax debts will apply.

## Detailed explanation of new law

2.5 The amendments enable amounts that are the balance of multiple taxation liabilities or credits to be allocated to a running balance account, and amounts within a running balance account to be transferred to a different running balance account. These amendments support the Commissioner accounting for income tax debts in a running balance account. *[Schedule 1, items 5 to 13, sections 8AAZA, 8AAZAA, 8AAZAB, 8AAZD and 8AAZDA of the TAA1953]*

2.6 For example, the Commissioner will be permitted to record the net amount payable from a notice of income tax assessment for an individual as one amount on the individual’s running balance account. This is in contrast to the Commissioner having to record primary tax liabilities such as income tax, the Medicare levy and the Medicare levy surcharge, and credits such as pay as you go withholding and instalments as separate amounts in a running balance account. Each liability and credit would still be separately listed on the individual’s notice of assessment.

2.7 The amendments also enable the Commissioner to transition existing tax accounts, including those accounts that are not maintained as running balance accounts, such as income tax accounts, to a running balance account. The Commissioner will be able to do this by determining the account balance is transitioned to a running balance account. This determination will have the effect that the tax debts, the general interest charge on those debts, and payments, credits and running balance account surpluses that correspond to the balance transferred will be treated as if it had been calculated under the running balance account rules. *[Schedule 1, item 14, sections 8AAZFA and 8AAZFB of the TAA1953]*

2.8 The broader use of running balance accounts, made possible through these amendments, will ensure taxpayers benefit from general interest charge being calculated on the daily balance of the account instead of separately on each primary tax liability.

## Application and transitional provisions

2.9 The amendments commence on the first day of the quarter following Royal Assent and apply from that date. *[Item 3 of the table in subclause 2(1) of the Exposure Draft]*