

From: John Kallinicos [REDACTED]
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To: Superannuation
Subject: Proposed Superannuation amendments

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Dear Sir/Madam,

I am a fully qualified accountant with over 40 years experience in public practice specialising in tax and accounting advice to individuals and small businesses. I also have substantial investments and run three businesses. In my time in public practise I have gained a wealth of knowledge and experience when it comes to financial matters in general.

It is difficult to understand the basis upon which the proposed superannuation changes are justified, however, it is fair to say that the proposed changes go well beyond a simple tax increase. The proposed changes seek to not only increase taxation but also to change the definition of income as we understand it. The concept of taxing unrealised gains seeks to redefine the definition of income. Not only do the new laws seek to tax unrealised gains but also increase the rate of tax applicable to the entire earnings of the fund as a consequence of the increased perceived market value of the assets of the fund with no regard to the liabilities of the fund. Seeking to determine the earnings of an entity based on asset values is without precedent and completely flawed.

The definition of income is a concept that has been fined tuned over many years both in the courts and through legislation. The accounting profession has for many years tried to fine tune the definition of income so as to provide more transparency and accurate assessment of an entity's earnings. From an accounting as well as a taxation perspective revenue is an inflow of money which is recurring and occurs regularly. One of the most contentious issues relating to net income is the timing of both income and expenses, and to this end both the courts and the legislators have endeavoured to develop clear laws so that the timing of income and expenses match one another. Income tax is based on net income which is determined by deducting allowable expenses from assessable income. The profitability of any entity has always been determined by the profit and loss statement. The profit and loss statement is the basis upon which the entire income tax assessment act is based yet the proposed new changes seek to completely disregard this basic principle and to replace it with a concept of perceived market value of gross assets based on someone's opinion. Net income of an entity is determined by the profit and loss statement and proven by the balance sheet. The proposed tax laws propose to ignore both the profit and loss statement and the balance sheet which is definitely a world first.

The proposed changes seek to completely disregard what has been developed over hundreds of years and replaced with a concept of taxing something which by definition is not revenue, is not recurring and does not take the form of cash. Furthermore it is not easily quantifiable because a transaction has not occurred. As for the concept of matching the timing of income and expenses, this concept is completely ignored because the cash expense namely the tax bill will occur annually yet the cash inflow/transaction namely the sale of the property (which in itself is not revenue) may not occur for 10 or 20 years if not more.

This creates many problems, including assessing an entities tax obligations based on an opinion as opposed to a fact. Secondly it seeks to levy a taxation not what has been received, but what is perceived as an increase in value. The problem is an increase in value cannot be spent nor can it be used to pay a tax bill nor will a bank provide funding to pay a tax bill. A simple assessment of the ramifications of the proposed legislation would frighten even the most seasoned of investors and tax advisors to the point where you would never use superannuation as an investment vehicle. Had we known that this was likely to ever occur nobody would ever use superannuation as a vehicle to fund one's retirement.

Superannuation funds are a trust and are a separate legal entity no different to any other trust or company. The only difference is that over the years successive governments have imposed more and more restrictions on the use of this type of investment vehicle which have reached the point where the structure itself has become unworkable and using a super fund as an investment vehicle is in fact a poor choice of structure and should only be used in limited circumstances.

It is fair to say the superannuation laws, as they now exist, lack all manner of commercial reality. Restrictions, such as limited capacity to borrow, investment restrictions, sole purpose test, limited capacity to deal with non-arms transactions, limited access to funds not to mention constant increases to the qualifying age and circumstances to access the funds are just a few of the reasons why I say superannuation laws lack commercial justification.

I will now move on to the ramifications of the proposed changes as they are being proposed. I will start with the concept of taxing an unrealised gain. Firstly, somebody has to assess the gain and while we already have to determine market values, the current ramifications of error or changes in market forces are relatively minor. The proposed laws are seeking to tax unrealised gains and to also set the tax rate based on the perceived value of the funds assets. This will result in an unfunded cash outgoing.

Let's consider the impact of taxing an unrealised gain to an asset that does not actually yield any form of cash income or very little cash income such as land, collectables & residential property. The reality is the super fund has to pay the tax however the super fund cannot borrow the money because its illegal and it has no income or very little income so instantly the fund is not only insolvent but non compliant. If we look at commercial and industrial real estate they are cyclical in nature meaning one minute their cash revenue is healthy and other times the revenue is reduced due to vacancies, inflationary trends and interest rates. During rising capital values vacancies tend to increase meaning increased unrealised gains but less income so how do we pay the tax bill? Even if you could borrow the money from a bank, banks normally do not fund tax bills. The only alternative is to sell assets and this is often a very slow process and in an emergency situation it becomes a fire sale.

As far as the proposed new taxes are concerned, one has to remember that these proposed taxes are not an increase of existing taxes, but rather an introduction of a completely new taxation regime. On top of this, they seek to redefine the definition of income which nobody has attempted to do in hundreds of years, therefore one can only question the analysis and thought process which has been applied to such a drastic change to the concept of income. While to many this would be meaningless to those of us who understand the concept of income versus capital it is certainly a frightening evolution of what I firmly believe is an ill-conceived, theoretical and a delusional concept. I cannot imagine any economist or accountant to be of the view that this is a sound evolution of the economy let alone the concept of taxation.

What has transpired is that people who were working within the laws of this country, and now being punished for being too successful and too frugal, and the government has the audacity to state that their success simply wasn't fair. The only thing that is not fair about this whole change to the taxation of superannuation funds is the proposed legislation itself.

In recent years, superannuation has become a political football, and both sides of politics who have taken upon themselves to manipulate the rules as they see fit. It is now abundantly clear that Investment via a superfund of any description is simply not an option because of the constant tinkering of the rules by politicians.

I note that politicians often argue that superannuation funds are tax advantaged but what they do not say is that there is a 17% tax bill once the money passes to a non dependant. If we add the new 15% tax as well as existing taxes it is fair to say that super funds pay up to 47% of tax making it the highest taxed entity in Australia. Add to this the fact that tax obligations are now being brought forward and applied to unrealised gains they are definitely the highest paying tax structure not to mention the worst structure from a compliance perspective.

I also note that statements have been made that super funds are being used as a way to escape tax through estate planning yet super is the only asset that gets taxed on death other than money left to dependants which in the majority of circumstances is your spouse and nobody else. Furthermore you cannot bequeath a member account it must be paid out to someone unless its your spouse and even then it must be transferred to his or her member account. So the suggestion that super is being used for estate planning is clearly false.

The fall out of the proposed changes is that nobody will have any confidence in the superannuation as a vehicle to retirement so it will at the end of the day dilute the use of super funds in general. The sad part is that the ones who will be most effected are the individual investors. The big end of town gave up on super a long time ago.


Why don't you start taxing multi nationals who transfer tax free money at will and make the beneficiaries of public funds accountable. This would be a much easier way of raising/save public funds as opposed to redefining the concept of income.

Best wishes

John Kallinicos – Director

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