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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

TAX LAWS AMENDMENT (SIMPLIFIED SUPERANNUATION) BILL 2006

SUPERANNUATION (EXCESS CONCESSIONAL CONTRIBUTIONS TAX) BILL 2006

SUPERANNUATION (EXCESS NON-CONCESSIONAL CONTRIBUTIONS TAX) BILL 2006

SUPERANNUATION (EXCESS UNTAXED ROLL-OVER AMOUNTS TAX) BILL 2006

SUPERANNUATION (DEPARTING AUSTRALIA SUPERANNUATION PAYMENTS TAX) BILL 2006

SUPERANNUATION (SELF MANAGED SUPERANNUATION FUNDS) SUPERVISORY LEVY AMENDMENT BILL 2006

EXPLANATORY MEMORANDUM

(Circulated by authority of the
Treasurer, the Hon Peter Costello MP)

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Glossary

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

Abbreviation	*Definition*
APRA	Australian Prudential Regulation Authority
ATO	Australian Taxation Office
CGT	capital gains tax
Commissioner	Commissioner of Taxation
ETP	eligible termination payment
FBT	fringe benefits tax
GIC	general interest charge
ITAA 1936	*Income Tax Assessment Act 1936*
ITAA 1997	*Income Tax Assessment Act 1997*
PAYG	pay as you go
RBL	reasonable benefit limit
RSA	retirement savings account
SG	superannuation guarantee
TAA 1953	*Taxation Administration Act 1953*
TFN	tax file number
This Bill	Tax Laws Amendment (Simplified Superannuation) Bill 2006

General outline and financial impact

Simplified superannuation

The Tax Laws Amendment (Simplified Superannuation) Bill 2006 (this Bill) and supporting Bills:

- implement the Government's *Simplified Superannuation* reforms; and

- rewrite the superannuation taxation law into the *Income Tax Assessment Act 1997* (ITAA 1997) to present a clear picture of the taxation of superannuation.

A simplified and streamlined superannuation system

The Government is sweeping away the current raft of complex tax arrangements and restrictions that apply to superannuation benefits. This will improve retirement incomes and increase incentives to work and save.

Schedule 1 to this Bill contains the key taxation elements of *Simplified Superannuation*. Broadly, the rules contained in Schedule 1:

- make superannuation benefits paid from a taxed fund either as a lump sum or a pension tax free for people aged 60 and over;

- lower the tax paid on superannuation benefits paid from an untaxed fund for people aged 60 and over;

- abolish reasonable benefit limits (RBLs);

- allow employers to claim a full tax deduction for contributions to superannuation on behalf of employees under the age of 75;

- allow the self-employed to claim a full tax deduction for contributions to superannuation up to age 75;

- limit the level of contributions to superannuation receiving concessional tax treatment to $50,000 per person per financial year; and
- limit personal superannuation contributions from an individual's post-tax income (known as non-concessional contributions) to $150,000 per financial year or $450,000 for a three year period.

Schedule 2 to this Bill limits concessions on large employment termination payments. Currently, both superannuation and employment termination payments are counted together in assessing if a person exceeds their RBL. As the RBL is to be removed for superannuation benefits, it is necessary to apply an upper limit on the amount of employment termination payments that receive concessional tax treatment.

Schedules 4 to 7 contain other key elements of *Simplified Superannuation*. Broadly, Schedules 4 to 7:

- streamline superannuation fund reporting requirements;
- extend access to the Government co-contribution to include the self-employed; and
- improve the regulation of self-managed superannuation funds through the application of new administrative penalties for late returns and false statements.

Schedules 8 and 9 halve the pension assets-test taper rate so that Age Pension, Service Pension and other pension recipients will only lose $1.50 a fortnight (rather than $3) for every $1,000 of assets above the relevant threshold. The 50 per cent assets-test exemption will be removed for 'complying' income streams purchased from 20 September 2007 as retaining this concession alongside the reduced assets-test taper would create scope for wealthier individuals to access the age pension.

Schedule 10 defines terms and Schedule 3 provides the method for indexing certain limits on contributions and tax thresholds.

The taxes on excess concessional and non-concessional contributions are introduced separately in the Superannuation (Excess Concessional Contributions Tax) Bill 2006 and the Superannuation (Excess Non-concessional Contributions Tax) Bill 2006. Similarly, a higher rate of tax on transfers over $1 million from untaxed to taxed schemes is introduced separately in the Superannuation (Excess Untaxed Roll-over Amounts Tax) Bill 2006. Each of these Bills deals with a separate object of taxation.

The Superannuation (Departing Australia Superannuation Payments Tax) Bill 2006 replaces the *Income Tax (Superannuation Payments Withholding Tax) Act 2002* to reflect the new components of superannuation benefits while retaining the same rates of taxation.

The Superannuation (Self Managed Superannuation Funds) Supervisory Levy Amendment Bill 2006 repeals the current penalty for the late lodgement of a self-managed superannuation fund's regulatory return.

Improved superannuation law

The provisions dealing with the taxation of superannuation in the *Income Tax Assessment Act 1936* (ITAA 1936) are being rewritten and consolidated into the ITAA 1997. This rewrite provides a clearer picture of the taxation treatment of superannuation savings across the life of the superannuation investment: when the money is contributed; during the investment phase; and at the benefit payment phase, and provides a consistent style.

The old legislation had become increasingly difficult to read and understand. When first introduced, the ITAA 1936 was only 126 pages. At that time, it was logically arranged and its sections were numbered in simple sequence. Since then the law has been heavily amended. Adding so much to the law has interfered with the logical arrangement of the sections and the numbering, making the ITAA 1936 difficult to navigate.

The new legislation deals first with the simple, most common case. For example, this means in the vast majority of cases the 90 per cent of Australians in taxed schemes would have their tax treatment specified in the first section about superannuation benefits if accessing their superannuation after age 60.

Preserving existing entitlements for those retiring between preservation age and age 60 and for the 10 per cent of Australians with benefits in untaxed schemes, means that some of the complexity and length of the old legislation has been retained. The user-friendliness of the legislation has however been greatly improved for these groups by the use of improved legislative design principles, such as plain English drafting and guides to groups of rules to aid reader navigation. In addition, sections are grouped on a case-by-case basis so a person can choose a path through the legislation.

Date of effect: *Simplified Superannuation* commences on 1 July 2007, although limits on non-concessional contributions apply from 10 May 2006. The revised age pension arrangements will commence on 20 September 2007.

Proposal announced: The proposals were released for community consultation on 9 May 2006 in *A Plan to Simplify and Streamline Superannuation*. The Government's final decisions were announced on 5 September 2006 in Press Release No. 93 issued jointly by the Treasurer and the Minister for Revenue and Assistant Treasurer.

Financial impact: The amendments in this Bill will have a budgetary cost of $7.2 billion over four years (including administration costs).

Impact on fiscal balance ($ billion)

2006-07	***2007-08***	***2008-09***	***2009-10***
–0.1	–2.2	–2.3	–2.6

Compliance cost impact: Initial implementation costs for individuals, employers and superannuation funds are expected to be offset by ongoing compliance savings from the new simplified and streamlined arrangements.

Summary of regulation impact statement

Impact: *Simplified Superannuation* will sweep away the raft of complex tax arrangements and restrictions that apply to superannuation benefits. These amendments will improve retirement incomes and increase incentives to work and to save.

The reforms will generate substantial improvements and savings for individuals, employers, superannuation funds and the Government, at the lowest cost.

Main points:

Individuals

- As a result of the Government's reforms, an average income earner whose sole contribution to superannuation comprises Superannuation Guarantee (SG) payments of 9 per cent over a working life of 40 years will have an additional lump sum of around $37,000 in retirement or an additional $136 per week if they take their benefit as a superannuation pension.
- Australians who turn 60 and choose to retire will have a much simpler system to face when deciding how to draw on their superannuation.
- The reduction in the assets-test taper rate will allow individuals to keep more of their pension when they exceed the relevant threshold.
- Individuals who make non-concessional contributions in excess of $150,000 per annum or $450,000 over a three year period will be affected by the limit on non-concessional contributions. However, the impact on these individuals will be mitigated through a number of exemptions and transitional arrangements.
- Individuals will have greater flexibility in how and when they take their superannuation benefits.
- The self-employed will benefit from improved incentives to contribute to superannuation, such as access to the superannuation co-contribution.
- Streamlined arrangements for individuals to find and transfer superannuation will encourage individuals to consolidate their accounts, thereby assisting in eliminating multiple fees and charges.

Employers

- Employers will benefit from their ability to claim a full deduction for superannuation contributions made on behalf of employees up to age 75.

- Employers who pay termination payments will benefit from a reduction in the number of forms required to process an employment termination payment entitlement. However, they will be required to update their existing systems to reflect the new employment termination payment tax arrangements.

Superannuation funds

- Superannuation funds will benefit from a reduction in the myriad of rules and red tape with which they must currently contend (eg, funds will no longer need to report benefits paid to members and commutations of pensions for RBL purposes). However, superannuation funds will incur implementation costs associated with adapting existing record-keeping systems and processes, training staff, updating product disclosure statements and communicating the changes to members.

- Simplified and streamlined pension rules will provide superannuation funds with greater scope to innovate. However, superannuation funds will also incur costs associated with communicating the streamlined rules to their members.

- Self-managed superannuation funds will benefit from simplified and streamlined reporting requirements and a suite of amendments designed to improve the level of education and assistance provided to self-managed superannuation fund trustees, and assist in the prevention and management of compliance problems. However, self-managed superannuation funds will face higher direct costs through an increase in the supervisory levy from $45 per annum to $150 per annum.

Government

- The Australian Taxation Office (ATO) will experience a reduction in the number of taxpayers who are required to lodge tax returns each year (around 152,000 taxpayers per annum based on 2004-05 tax return data) as a result of the abolition of end benefits tax.

- The ATO will require additional resourcing to develop new information technology systems, update its technical and information products (electronic and printed), and manage the increased administrative workflow resulting from the new contribution rules and arrangements to assist individuals in locating their 'lost' superannuation accounts.

Chapter 1
Contribution rules

Outline of chapter

1.1 Schedule 1 to this Bill provides tax concessions for contributions to superannuation, imposes tax on contributions in excess of specified thresholds and details the administrative arrangements for excess contributions tax. The tax will be introduced in the *Superannuation (Excess Concessional Contributions Tax) Act 2006* and the *Superannuation (Excess Non-concessional Contributions Tax) Act 2006* to ensure each Bill deals with a separate object of taxation.

1.2 All legislative amendments are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated.

Context of amendments

1.3 Currently, employer contributions (ie, through superannuation guarantee (SG) and salary sacrifice arrangements) are subject to tax in the superannuation fund. Employers can claim a tax deduction for these contributions up to the employee's age-based deduction limits.

1.4 Taxable contributions include both deductible and undeducted employer contributions. An example of an undeducted employer contribution is where an employer makes a contribution above an individual's age-based limit.

1.5 Personal contributions are also subject to tax when they are deductible, for example when made by self-employed individuals and certain other eligible persons. A full deduction is currently available for the first $5,000 contributed to superannuation and a deduction is available for 75 per cent of the remaining amount up to a maximum deduction equal to the individual's age-based limit.

1.6 Some other less common contributions to superannuation (ie, those made by a friend) are also subject to tax.

1.7 These contributions are currently referred to as taxable contributions but will be referred to in this Bill as assessable contributions. Under the current law, and in this Bill, these contributions are, and will be, included in the assessable income of the superannuation provider and subject to the applicable rate of tax (for complying funds this rate is 15 per cent).

1.8 Currently, personal contributions for which a tax deduction is not claimed are commonly referred to as undeducted (or post-tax) contributions. However, in this Bill they will be referred to as non-concessional contributions. Under the current law, and in this Bill, these contributions are not, and will not be, included in the assessable income of the superannuation provider. Currently, there are also no limits on the amount of undeducted contributions that can be made in a year.

Summary of new law

1.9 The object of this Schedule is to ensure that the amount of concessionally taxed superannuation benefits that a person receives results from superannuation contributions that have been made gradually over the course of the person's life.

1.10 From 1 July 2007, employers will be entitled to a full deduction for all contributions to superannuation on behalf of their employees provided certain conditions are met. In addition, the self employed (and other eligible individuals) will also be entitled to a full deduction. That is, the limiting of the deduction for personal contributions to 75 per cent of the contribution above $5,000 up to the person's age-based limits will be abolished.

1.11 The removal of age-based deduction limits, reasonable benefit limits (RBLs) and tax on superannuation benefits from taxed funds for people 60 and over will increase the concessions provided to superannuation. These changes, in conjunction with the continuing tax exemption provided for income from superannuation assets supporting a pension, will make superannuation an attractive vehicle for retaining assets to minimise tax. There will be an incentive for people to transfer

income producing assets currently held outside superannuation to the concessionally taxed superannuation system.

1.12 To ensure superannuation taxation concessions are targeted appropriately, limits will be placed on the amount of superannuation contributions a person can make that receive concessional treatment. In addition, this Bill replaces the current tax arrangements for deductible contributions with a streamlined set of rules.

Concessional contributions

1.13 From 1 July 2007, the amount of concessional (generally assessable) contributions that will benefit from the concessional tax treatment will be capped at $50,000 per person per year.

1.14 Contributions in excess of this cap will be taxed at an additional 31.5 per cent. This tax will be imposed on the individual, who will be able to withdraw from their superannuation fund an amount equal to their tax liability.

1.15 A five year transitional cap of $100,000 per person per year (for the financial years 2007-08 to 2011-12) will apply for people who are aged 50 and over on the last day of a financial year in that period.

Non-concessional contributions

1.16 A cap of $150,000 a year on the amount of non-concessional (generally undeducted) contributions a person can make will apply from 1 July 2007.

1.17 As a concession, to accommodate larger contributions, people under age 65 will be able to bring forward future entitlements to two years worth of contributions, giving them a cap of $450,000 over three years.

1.18 Non-concessional contributions in excess of a person's cap will be taxed at 46.5 per cent. This tax will be imposed on the individual, who *must* withdraw an amount from their superannuation fund equal to their tax liability.

1.19 Certain contributions arising from payments for personal injuries that result in permanent incapacity and amounts of up to a lifetime indexed limit of $1 million from the disposal of qualifying small business assets will *not* be counted towards the cap on non-concessional contributions.

1.20 However, as an integrity measure, excess concessional contributions *will* also be counted towards the cap on non-concessional contributions.

1.21 Transitional arrangements will apply to non-concessional contributions made between 10 May 2006 and 30 June 2007. This includes a cap of $1 million for this period for anyone eligible to contribute (eg, those aged 65 to 74 who satisfy the work test).

Comparison of key features of new law and current law

New law	*Current law*
Deductible contributions	
Full deductibility for both employers and those who qualify for deductions for personal contributions. A cap of $50,000 per year on concessional contributions for all ages (with a five year transitional cap of $100,000 per year for people aged 50 and over). Individuals will be subject to tax on contributions in excess of these caps at an additional 31.5 per cent.	Employers receive a full tax deduction on amounts up to the employee's indexed age based limits. For 2006-07 these are: Age — Deduction limit Under 35 — $15,260 p.a. 35 to 49 — $42,385 p.a. 50 and over — $105,113 p.a. The self-employed (and other eligible persons) receive a full deduction for the first $5,000 of contributions and a 75 per cent deduction on amounts above this up to a maximum deduction equal to the age-based limit.
Other assessable (taxable) contributions	
Contribution made on behalf of someone else but no deduction is allowed to the contributor and not excluded from being assessable contributions. Included in the $50,000 on concessional contributions ($100,000 transitional cap	Contribution made on behalf of someone else but no deduction is allowed to the contributor and not excluded from being taxable contributions.

New law	*Current law*
for people aged 50 and over) and contributions in excess are taxed as above.	
Non-concessional contributions and amounts (including undeducted contributions)	
A cap on non-concessional contributions of $150,000 a year from 1 July 2007. Other non-concessional contributions and amounts include contributions that exceed the concessional contributions cap. Contributions totalling up to $450,000 in one year are allowed by bringing forward future entitlements to two years worth of contributions. A transitional cap of $1 million on non-concessional contributions made between 10 May 2006 and 30 June 2007. Individuals will be subject to tax on contributions in excess of the cap at 46.5 per cent. Exemptions are provided for certain contributions made from amounts from the sale of qualifying small business assets and from settlements resulting from personal injuries.	No limits on undeducted contributions made in a year.

Detailed explanation of new law

Tax concessions for superannuation contributions

1.22 As part of the Government's *Simplified Superannuation* reforms, the provisions relating to tax concessions for contributions to superannuation entities are being rewritten and consolidated in Division 290 of the ITAA 1997.

1.23 Taxpayers can obtain a deduction or an offset for contributions to a complying superannuation fund or retirement savings account (RSA). The circumstances in which a deduction or offset is available vary depending on who is making the

contribution, who the contribution is made for, and the status of the fund to which the contribution is made.

1.24 Superannuation contributions to either a complying or a non-complying superannuation fund will not be able to be deducted under provisions elsewhere in the *Income Tax Assessment Act 1936* (ITAA 1936) or the ITAA 1997. However, other provisions of the income tax law may vary the deduction available (eg, subsection 73B(14) of the ITAA 1936, which applies to certain superannuation contributions paid in respect of an employee engaged in research and development activities). ***[Schedule 1, item 1, section 290-10]***

1.25 Certain contributions will not be eligible for a tax deduction under Division 290. These contributions include:

- the roll-over of superannuation benefits ***[Schedule 1, item 1, section 290-5]***;
- a benefit transferred from an overseas superannuation fund ***[Schedule 1, item 1, section 290-5]***; or
- a directed termination payment paid into a superannuation plan by an employer under transitional arrangements that apply until 30 June 2012 ***[Schedule 1, item 25, section 290-10 of the Income Tax (Transitional Provisions) Act 1997]***.

Employer contributions

1.26 Employers are entitled to a full deduction for all contributions to superannuation on behalf of employees provided certain conditions are met. A deduction is allowable only for the year in which the contribution is made. ***[Schedule 1, item 1, section 290-60]***

1.27 The contribution must be for the purpose of providing superannuation benefits for the employee. The contribution will still be deductible, even if these benefits are payable to dependants of the employee (or their legal personal representative) after the death of the employee. However, no deduction is available under this provision for a contribution made in respect of an employee who has died, unless the conditions in new section 290-85 are satisfied (see paragraph 1.39). ***[Schedule 1, item 1, section 290-60]***

1.28 The personal services income rules in Part 2-42 of the ITAA 1997, which can affect the tax deductibility of superannuation contributions, will continue to apply. These rules may disallow or limit deductions on contributions made for the benefit of an associate (such as a spouse).

1.29 A contribution made under the *Family Law Act 1975* to satisfy the entitlement of a former spouse (who may also be an employee) will continue not to be an allowable deduction. ***[Schedule 1, item 1, subsection 290-60(4)]***

Who is an employee?

1.30 The existing expanded definition of 'employee' given by section 12 of the *Superannuation Guarantee (Administration) Act 1992* is maintained. For example, the expanded definition ensures a person who works under a contract that is wholly or principally for their labour is an employee. ***[Schedule 1, item 1, subsection 290-65(1)]***

1.31 A partner who makes a contribution for an employee of the partnership can deduct the contribution against their own income, even though the partner is not strictly the employer. This does not limit the ability of the partnership to claim a tax deduction when it makes a superannuation contribution on behalf of the same employee. However, a partner and the partnership cannot claim a tax deduction in respect of the same contribution. ***[Schedule 1, item 1, subsection 290-65(2)]***

1.32 The wording in the above provisions has been amended to improve readability. This rewording does not modify the operation of the existing law.

What conditions must be met?

1.33 The conditions that must be met for employer contributions to be deductible have been simplified by removing the age-based deduction limits. In addition, employers may receive a full tax deduction for all contributions to superannuation on behalf of employees under the age of 75 (increased from the current age 70). This will allow more older employees to enter into superannuation salary sacrifice arrangements. ***[Schedule 1, item 1, section 290-80]***

1.34 Employers will only be able to claim a deduction for contributions to superannuation for employees aged 75 and over if those contributions are required to be made under an industrial award, determination or notional agreement preserving State awards. ***[Schedule 1, item 1, section 290-80]***

1.35 Conditions for the contribution to be deductible in the existing legislation that have been maintained are that:

- the employee must be engaged in producing assessable income of the employer or an Australian resident who is engaged in the employer's business ***[Schedule 1, item 1, section 290-70]***; and
- the superannuation fund is a complying superannuation fund or, if the fund is not complying, the employer reasonably believed the fund was complying or obtained a written statement from the fund stating that it was a resident regulated superannuation fund and not subject to a direction preventing it from accepting employer contributions ***[Schedule 1, item 1, section 290-75]***.

Contributions for former employees

1.36 The general deduction rules outlined above are modified in certain circumstances for contributions made for former employees.

1.37 Superannuation contributions for former employees would ordinarily not be deductible because a condition for deductibility is that the contribution is made at a time when the individual is an employee. However, contributions for former employees that reduce an employer's SG charge percentage (ie, to meet an SG obligation) will continue to be deductible provided the other conditions for deductibility are present. ***[Schedule 1, item 1, section 290-85]***

1.38 This Bill also provides that a deduction is available for a superannuation contribution made on behalf of a former employee if the contribution is made in lieu of salary or wages (under a salary sacrifice arrangement) and relates to a period of service during which the person was an employee. The contribution has to be a one-off payment made following termination of

employment and should reflect the employee's normal contributions to superannuation just before they ceased employment. ***[Schedule 1, item 1, section 290-85]***

Example 1.1

> Andrew entered into a salary sacrifice arrangement during his employment under which 20 per cent of his salary was contributed to superannuation. Andrew resigns from his job on 1 December 2007 when he is age 50. His final pay period ends on 20 December 2007. The 20 per cent of Andrew's final pay that is contributed to a complying superannuation fund on 20 December is an allowable deduction to his former employer (no other contribution is made after his resignation).

1.39 Deductions will also be available for superannuation contributions made after the death of an employee in the above circumstances (ie, to satisfy an SG obligation or under a salary sacrifice arrangement).

Contributions made by persons with a controlling interest

1.40 The general deduction rules are also modified for certain circumstances where superannuation contributions are made by an entity other than an employer. For example, deductions may be available to a person with a controlling interest in the employer. This modification has been maintained from the existing legislation and, although the wording has been updated, it is not intended to modify the operation of the existing law. ***[Schedule 1, item 1, section 290-90]***

Contributions to offset the superannuation guarantee charge

1.41 A charge imposed under the *Superannuation Guarantee Charge Act 1992* is not tax deductible. Therefore, a contribution that is offset against a SG charge liability cannot be deducted. The wording of this provision has been modified to improve readability. This rewording is not intended to modify the operation of the existing law. ***[Schedule 1, item 1, section 290-95]***

Returned contributions

1.42 Returned contributions, and earnings on those contributions, are assessable income to the recipient if they have previously been deductible to the employer under new Subdivision

290-B of the ITAA 1997 or section 82AAC of the ITAA 1936, unless they are received as a superannuation benefit. The wording of this provision has been modified to improve readability. This rewording is not intended to modify the operation of the existing law. Consistent with existing law, the provision does not apply to personal contributions. ***[Schedule 1, item 1, section 290-100]***

Personal contributions

1.43 The self-employed (and other eligible individuals) can currently deduct personal contributions if they are not entitled to receive superannuation support as an employee from another person (eg, an employer) or if that superannuation support is attributable to less than 10 per cent of their assessable income and reportable fringe benefits for the year.

1.44 From 1 July 2007, the self-employed (and other eligible individuals) will be entitled to a full deduction for superannuation contributions provided certain conditions are met. The deduction is only available in the income year in which the contribution is made. ***[Schedule 1, item 1, section 290-150]***

1.45 An individual's contribution must be for the purpose of providing superannuation benefits for themself. Like employer contributions, the contribution will still be deductible even if these benefits are payable to their dependants (or legal personal representative) after their death. ***[Schedule 1, item 1, section 290-150]***

What conditions must be met?

1.46 A person can deduct personal contributions, even if they receive some income as an employee. Currently, eligibility to deduct contributions is determined by the percentage of earnings on which superannuation support is obtained. This test will be simplified by making it consistent with the rule that currently applies for the Government co-contribution. ***[Schedule 1, item 1, section 290-160]***

1.47 Personal contributions will be deductible if less than 10 per cent of a person's assessable income and reportable fringe benefits are attributable to employment as an employee. The test will no longer be determined by the level of employer superannuation support a person receives or should have received. ***[Schedule 1, item 1, section 290-160]***

1.48 The self-employed person (or other eligible individual) must be under the age of 75 (increased from the current age 70) in order to receive a tax deduction. This will allow older individuals who meet the work test to make deductible contributions to superannuation. ***[Schedule 1, item 1, subsection 290-165(2)]***

1.49 To be eligible for the deduction, individuals must have given a notice to the trustee or RSA provider of their intention to claim a deduction by a certain time, and received an acknowledgment from the trustee or RSA provider of receipt of the notice. ***[Schedule 1, item 1, sections 290-170 to 290-175]***

1.50 Conditions for the contribution to be deductible that have been maintained in the existing legislation are:

- The superannuation fund must be a complying superannuation fund ***[Schedule 1, item 1, section 290-155].***
- Individuals under the age of 18 must have derived income from being an employee or carrying on a business ***[Schedule 1, item 1, subsection 290-165(1)].***

Notice requirements

1.51 An individual who wishes to claim a tax deduction for their superannuation contributions will continue to be required to notify the trustee or RSA provider in writing. The notice arrangements are being revised to ensure that the Australian Taxation Office (ATO) will have the relevant information to administer the new contribution caps (ie, the concessional contributions cap and the non-concessional contributions cap) and to determine eligibility for the co-contribution, following extension of the co-contribution to the self-employed.

1.52 This notice will now be required to be given by the earlier of the time the person lodges their income tax return or the end of the financial year following the year the contribution was made. This notice may be varied in limited circumstances (see paragraph 1.58). This will assist the Commissioner of Taxation (Commissioner) administration of the new contribution caps, and reduce the administrative burdens on superannuation funds and RSAs. ***[Schedule 1, item 1, section 290-170]***

1.53 A notice will not be valid in certain circumstances. These circumstances have been expanded to include when a notice is

given to the trustee or RSA provider, where it either no longer holds the contribution or has begun to pay a superannuation income stream that includes the contribution. ***[Schedule 1, item 1, subsection 290-170(2)]***

1.54 An example of when the trustee or RSA provider no longer holds a contribution is where the member has requested a partial roll-over of the superannuation benefit which includes the contribution covered in the notice.

Example 1.2

> Rachel's superannuation interest is valued at $5,000 (tax free component). She makes a $10,000 personal contribution in March 2008 which would be counted against the tax free component of her superannuation interest at the time it is received. Her total superannuation account balance is $15,000.
>
> In June 2008, Rachel requests to roll-over $6,000 leaving her with a balance of $9,000. She then lodges a notice in September 2008 advising that she intends to claim a deduction on the $10,000 contribution made in the 2007-08 income year.
>
> As her account balance is only $9,000, all of the $10,000 contribution is no longer held by the trustee and therefore the notice is not valid. However, if Rachel were to lodge a notice for $9,000, this would be valid. The trustee would then convert the $9,000 from a tax free component to a taxable component and include this amount in the fund's assessable income.

1.55 If the trustee or RSA provider has merely transferred its tax liability to a life insurance company or pooled superannuation trust under new section 295-260, it will still hold the contribution.

1.56 The trustee or RSA provider will continue to be required to acknowledge the receipt of a valid notice. ***[Schedule 1, item 1, subsection 290-170(3)]***

1.57 To ensure that other members of the superannuation fund are not disadvantaged, the superannuation provider can refuse to acknowledge a notice if the value of the person's superannuation interest is less than the tax that the fund would pay if it acknowledged the notice. ***[Schedule 1, item 1, subsection 290-170(4)]***

Variation requirements

1.58 A notice cannot be revoked or withdrawn but may be varied to reduce the amount covered by the notice (including to nil) before the earlier of the time the person lodges their income tax return or the end of the financial year following the year the contribution was made. After this time, the notice cannot be varied unless a deduction is not allowable, as demonstrated by the following examples. ***[Schedule 1, item 1, section 290-180]***

Example 1.3

John lodges a valid notice to claim a tax deduction for a personal contribution of $5,000 made during the 2007-08 income year. His superannuation fund acknowledges this notice and in his 2007-08 income tax return John claims a tax deduction for $5,000. John satisfies all the conditions for claiming a deduction for his personal contribution.

However, after lodging his income tax return, John requests an amendment to vary the amount claimed as a tax deduction to $3,000. As the $5,000 deduction is allowable to John, he will not be able to vary the amount to $3,000.

Example 1.4

Samantha lodges a valid notice to claim a tax deduction for a personal contribution of $8,000 made during the 2007-08 income year. Her superannuation fund acknowledges this notice in her 2007-08 income tax return and she claims a deduction for $8,000. Samantha satisfies all the conditions for claiming a tax deduction for her personal contribution.

Samantha's assessable income for the year is $5,000. She has no other deductions apart from the personal superannuation contribution deduction. A deduction is not allowable for $3,000 of the contribution since this is the amount by which the contribution exceeds her assessable income. Samantha may apply to her superannuation fund to vary her notice, reducing the amount covered by the notice to $5,000.

Spouse contributions

1.59 Taxpayers will continue to be entitled to claim an 18 per cent tax offset on superannuation contributions of up to $3,000 made on behalf of their low income spouse under the current

arrangements. With the receiving spouse's consent the contributing spouse may quote their tax file number. ***[Schedule 1, item 1, sections 290-230 to 290-240]***

1.60 The wording of these provisions has been modified to improve readability. This rewording does not modify the operation of the existing law.

Tax on excess contributions

Overview

1.61 Superannuation contributions will be subject to annual caps. Contributions in excess of the relevant caps will be subject to additional tax. This tax will be imposed on individuals. Where an excess contributions tax liability arises, the individual will be able to, and in some cases *must*, withdraw an amount equal to their tax liability from their superannuation fund.

1.62 Transitional provisions have been put in place to accommodate the commencement of the cap on non-concessional contributions from 10 May 2006. These include a cap of $1 million applying until 30 June 2007 for anyone eligible to contribute and a limited discretion being given to the Commissioner to allow the removal of excess contributions made prior to 7 December 2006 without penalty.

Concessional contributions cap

1.63 A cap of $50,000 per person per year applies to concessional contributions from 1 July 2007. This cap will be indexed. Excess concessional contributions tax is payable on any concessional contributions over the concessional contributions cap for a financial year. ***[Schedule 1, item 1, sections 292-15 and 292-20]***

What are concessional contributions?

1.64 An individual's concessional contributions in a financial year are generally contributions made by or for that individual in that year that are included in the assessable income of a superannuation provider. The contributions do not have to be included in the assessable income of the superannuation provider in the same year as the contribution is made. ***[Schedule 1, item 1, section 292-25]***

1.65 An individual's concessional contributions do *not* include:

- roll-over superannuation benefits to the extent that they consist of an element untaxed in the fund of the taxable component in the transferring fund ***[Schedule 1, item 1, subparagraph 292-25(2)(c)(ii)]***;
- up to $1 million of directed termination payments specified in employment contracts as at 9 May 2006, provided the payment is made prior to 1 July 2012. The $1 million is reduced by any earlier transitional termination payments that are received ***[Schedule 1, item 25, section 292-25]***;
- the amount of a superannuation benefit transferred from a foreign superannuation fund to which an election under subsection 307-50(2) applies. This component generally reflects investment earnings on overseas superannuation benefits while the individual was an Australian resident ***[Schedule 1, item 1, subparagraph 292-25(2)(c)(i)]***; or
- any contributions made to constitutionally protected superannuation funds. The taxable component of a superannuation benefit paid by a constitutionally protected superannuation fund can only consist of an element untaxed in the fund which is subject to separate taxation arrangements (see Chapter 2) ***[Schedule 1, item 1, subparagraph 292-25(2)(c)(iii)]***.

1.66 To ensure the integrity of the concessional contributions cap, regulations may contain rules specifying that additional amounts allocated to an individual by the superannuation provider can also be included. These amounts will be included in an individual's concessional contributions cap if they exceed an amount that reasonably reflects the contribution made by, or on behalf of, the individual and investment earnings in relation to the individual's superannuation interest. For example, large amounts paid into reserves and then allocated to members in an attempt to circumvent the cap will be counted in the year that they are allocated. ***[Schedule 1, item 1, subsection 292-25(3)]***

1.67 Contributions excluded from the assessable income of superannuation providers, including the transfer of taxation liabilities and the application of pre-1 July 1988 funding credits (under Subdivision 295-D of the ITAA 1997) do not reduce the amount of assessable contributions included in a person's concessional contributions cap for the purposes of this Subdivision. ***[Schedule 1, item 1, subsection 292-25(4)]***

1.68 Whilst payments from the Commissioner under the *Superannuation Guarantee Administration Act 1992* or the *Small Superannuation Accounts Act 1995* are assessable, and therefore concessional contributions if contributed after 1 July 2007, a person will be able to apply to the Commissioner to exercise discretion to disregard those amounts to the extent that they relate to employer contributions that should have been made before 1 July 2007. ***[Schedule 1, item 1, sections 292-25 and 292-465]***

Transitional arrangements for concessional contributions

1.69 A transitional concessional contributions cap of $100,000 per person per year will apply in the financial years 2007-08 to 2011-12 for individuals aged 50 or over at any time in a transitional financial year. This cap will not be indexed. ***[Schedule 1, item 25, section 292-20 of the Income Tax (Transitional Provisions) Act 1997]***

Example 1.5

Jeremy turns 50 on 5 October 2009 (in the 2009-10 financial year). At this time, he becomes entitled to the higher transitional cap of $100,000 per year. His annual concessional contributions caps for the years 2007-08 to 2011-12 are set out in the table below.

Financial year (age)	***2007-08 (48)***	***2008-09 (49)***	***2009-10 (50)***	***2010-11 (51)***	***2011-12 (52)***
Annual concessional contributions cap	$50,000	$50,000	$100,000	$100,000	$100,000

Modifications to concessional contributions for defined benefit interests

1.70 Separate arrangements for calculating concessional contributions in relation to defined benefit superannuation interests are necessary because employer contributions made into these interests are not always attributable to individual members.

1.71 A defined benefit interest exists where all or part of the superannuation benefits payable are defined by reference to the salary or average salary of the person (or of another person), a specified amount or specified conversion factors. ***[Schedule 1, item 1, subsection 292-175(1)]***

1.72 Some superannuation plans may pay death or disability benefits that are referenced to the member's salary. However, a superannuation interest is not a defined benefit interest if the only benefits payable in reference to a salary (or other matters outlined above) are death or disability benefits. ***[Schedule 1, item 1, subsection 292-175(2)]***

1.73 The concessional contributions amount for a defined benefit interest will be referred to as notional taxed contributions. The method for calculating notional taxed contributions will be set out in the regulations to this legislation. The regulations may allow for different methods depending on various matters and may specify circumstances where the notional taxed contributions amount for a financial year is nil. ***[Schedule 1, item 1, section 292-170]***

1.74 Where only part of an interest is a defined benefit interest, the concessional contributions cap includes notional taxed contributions in respect of the defined benefit part of the interest and contributions covered under section 292-25 in respect of the rest of the interest. ***[Schedule 1, item 1, section 292-165]***

Grandfathering certain defined benefit interests

1.75 Given the unique nature of defined benefit interests, and the difficulty for members to reduce their contributions or notional taxed contributions, certain arrangements will be grandfathered so that these members are not unfairly taxed under the excess concessional contributions cap. ***[Schedule 1, item 1, subsection 292-170(6)]***

1.76 Special arrangements will apply to members with a defined benefit interest on 5 September 2006 with notional taxed

contributions for that interest that exceed the concessional contributions cap. In this case, the notional taxed contributions for that interest will be taken to be at the maximum level of the cap. This arrangement will cease to apply if the scheme amends their rules to increase the member's benefits. ***[Schedule 1, item 1, subsection 292-170(6)]***

1.77 However, the regulations may allow for some changes to the rules of the superannuation fund to be permitted, even if they increase member benefits. For example, schemes may be able to amend their rules to meet requirements in other legislation without members losing access to this grandfathered arrangement. ***[Schedule 1, item 1, paragraph 292-170(6)(d)]***

Example 1.6

> Some employers are currently able to pay lower SG contributions for their employees as a result of pre-21 August 1991 earnings bases.
>
> From 1 July 2008, the use of a pre-21 August 1991 earnings base to calculate the employer's contribution for SG will no longer be allowed. From that date the employer must use ordinary times earnings to determine their SG liability. Although this will result in the employee's benefit increasing it will not result in the member losing access to the grandfathering arrangements.

1.78 In addition, the grandfathered arrangement will continue to apply if the defined benefit interest is transferred to a successor superannuation fund that retains equivalent rights for members. ***[Schedule 1, item 1, subsection 292-170(7)]***

Non-concessional contributions cap

1.79 A cap of $150,000 per person per year on non-concessional contributions will apply from 1 July 2007. Rather than being separately indexed, this cap will remain fixed at three times the ongoing concessional contributions cap. Excess non-concessional contributions tax is payable on non-concessional contributions over the non-concessional contributions cap for a financial year. ***[Schedule 1, item 1, section 292-80 and subsections 292-85(1) and (2)]***

1.80 A person who qualifies for the transitional concessional cap of $100,000 per year will *not* have a non-concessional cap of $300,000. ***[Schedule 1, item 25, subsection 292-20(3)]***

What are non-concessional contributions?

1.81 An individual's non-concessional contributions in a financial year are generally contributions made by or for that individual in that year that are *not* included in the assessable income of a superannuation provider. ***[Schedule 1, item 1, section 292-90]***

1.82 Contributions made directly by an individual into their spouse's account will be counted against the receiving spouse's non-concessional contributions cap.

1.83 In addition, the following amounts are also included:

- excess concessional contributions. This ensures that people cannot circumvent the caps by making excess concessional contributions ***[Schedule 1, item 1, paragraph 292-90(1)(b)]***; and
- contributions made to a constitutionally protected fund that, had the constitutionally protected fund been a taxed fund, would not have been taxed in the fund anyway ***[Schedule 1, item 1, subparagraph 292-90(2)(c)(iv)]***.

1.84 However, an individual's non-concessional contributions do *not* include:

- a Government co-contribution ***[Schedule 1, item 1, subparagraph 292-90(2)(c)(i)]***;
- certain contributions relating to personal injury payments and amounts from the disposal of certain small business assets ***[Schedule 1, item 1, subparagraphs 292-90(2)(c)(ii) and (iii)]***;
- contributions that are paid out as a superannuation benefit in the same year that they are contributed as an element untaxed in the fund ***[Schedule 1, item 1, subparagraph 292-90(2)(c)(v)]***;
- a roll-over superannuation benefit ***[Schedule 1, item 1, subparagraph 292-90(2)(c)(vi)]***; and
- amounts not included in a provider's assessable income because of Subdivision 295-D. These amounts are

included in a person's concessional contributions cap ***[Schedule 1, item 1, subsection 292-90(3)].***

Bring forward

1.85 As a concession, to accommodate larger contributions, people under age 65 in a financial year will be able to bring forward future entitlements to two years worth of non-concessional contributions. This means a person under age 65 will be able to contribute non-concessional contributions totalling $450,000 over three financial years without exceeding their non-concessional contributions cap. ***[Schedule 1, item 1, subsections 292-85(3) and (4)]***

1.86 The bring forward will be triggered automatically when contributions in excess of the annual non-concessional contributions cap are made in a financial year by a person who is under age 65 at any time in the year where a bring forward has not already commenced. ***[Schedule 1, item 1, subsection 292-85(3)]***

1.87 Where a bring forward has been triggered, the two future years' entitlements are not indexed. ***[Schedule 1, item 1, subsection 292-85(4)]***

1.88 Table 1.1 sets out the operation of the bring forward. For simplicity, the effect of indexation (where relevant) is not reflected in the table.

Table 1.1

Year	*Scenario 1*	*Scenario 2*	*Scenario 3*	*Scenario 4*
Year 1	Less than $150,000 Bring forward not triggered in this year.	Between $150,001 and $449,999 Bring forward triggered in this year.	$450,000 Entire bring forward entitlement used in this year.	More than $450,000 A tax liability for the excess in this year.
Year 2	Up to $150,000 per year or $450,000 over	Up to the difference between contributions in Year 1 and	Additional non-concessional contributions before Year 4 will exceed the	Additional non-concessional contributions before Year 4 will exceed the

	three years.	$450,000 over Years 2 and 3.	cap and result in a tax liability.	cap and result in a further tax liability.
Year 3				
Year 4		Up to $150,000 per year or $450,000 over three years.	Up to $150,000 per year or 450,000 over three years.	Up to $150,000 per year or $450,000 over three years.

1.89 To simplify the operation of the non-concessional contributions cap, people aged 63 and 64 who take advantage of the bring forward will not be required to meet the work test in either of the following two financial years.

1.90 People aged 65 to 74 will have a non-concessional contributions cap of $150,000 per year provided they satisfy the work test set out in the *Superannuation Industry (Supervision) Regulations 1994*. Not allowing people over 65 to bring forward entitlements to non-concessional contributions will ensure people do not inadvertently breach the cap by failing to meet the work test in the following two financial years.

Example 1.7

Linda is 64 years old and makes contributions of $450,000 to her superannuation funds in the 2007-08 financial year. Linda does not have to satisfy the work test in either of the following two financial years in respect of the $450,000 contributions made under the bring forward arrangements.

From 2008-09, being 65, Linda will have to satisfy the work test in order to make contributions. Any additional non-concessional contributions Linda makes before 1 July 2010 will be in excess of her cap and will result in a tax liability.

If Linda satisfies the work test in the 2010-11 financial year she will have a non-concessional contributions cap for that year of $150,000. Contributions in excess of $150,000 will exceed her cap and will result in a tax liability. Being over 65, she will not be able to bring forward future entitlements to increase her cap (as she did in 2007-08).

Example 1.8

Glenn, aged 49, makes contributions totalling $160,000 in a year. Having not already triggered the bring forward in the previous two years, a bring forward would now be triggered.

Glenn can make additional contributions of $390,000 over the following two years without having excess contributions. However, if contributions in that period exceed $390,000 Glenn will be taxed on the excess contributions at 46.5 per cent.

If Glenn makes contributions of less than $390,000 in those two years he will lose the entitlement to them. That is, they can not be carried forward for use in future years.

Exemptions to the non-concessional contributions cap

1.91 In conjunction with the commencement of the non-concessional contributions cap from 10 May 2006, there are two ongoing exemptions to the cap. These relate to contributions arising from certain payments for personal injuries that result in permanent incapacity and amounts from the disposal of qualifying small business assets.

Payments for personal injury

1.92 Contributions made from certain personal injury payments are exempt from the non-concessional contributions cap when contributed to superannuation if no tax deduction is claimed. ***[Schedule 1, item 1, section 292-95]***

1.93 The personal injury payment must be in the form of a structured settlement, an order for a personal injury payment, or lump sum workers compensation payment. ***[Schedule 1, item 1, paragraph 292-95(1)(a)]***

1.94 Two legally qualified medical practitioners must certify that the person is unlikely to ever be able to be gainfully employed in a capacity for which they are reasonably qualified as a result of the injury. ***[Schedule 1, item 1, paragraph 292-95(1)(c)]***

1.95 The individual must notify the superannuation provider that the contribution is being made under this exemption before, or when, making the contribution. This will ensure that the superannuation provider is able to accept the contribution and that

it is not reported against the non-concessional contributions cap. ***[Schedule 1, item 1, paragraph 292-95(1)(d)*]**

1.96 The contribution must be made to a superannuation fund within 90 days of the payment being received or the structured settlement or order coming into effect, whichever is later. ***[Schedule 1, item 1, paragraph 292-95(1)(b)]***

1.97 The exemption from the non-concessional contributions cap only applies to the extent that the payment received relates to an amount for personal injury. ***[Schedule 1, item 1, subsection 292-95(5)]***

Amounts from the disposal of qualifying small business assets

1.98 Contributions made from certain amounts arising from the disposal of qualifying small business assets are exempt from the non-concessional contributions cap of a person up to a lifetime limit of $1 million (indexed) where the amount is not included in the assessable income of the superannuation provider (ie, it must be a personal contribution for which no deduction is claimed). This amount is referred to as the capital gains tax (CGT) cap. ***[Schedule 1, item 1, section 292-105]***

1.99 Contributions allowed under the CGT cap are:

- up to $500,000 of capital *gains* that are disregarded under the CGT exemption in Subdivision 152-D ***[Schedule 1, item 1, subsection 292-100(7)].*** This supports the underlying CGT exemption which requires that capital gains which are disregarded under Subdivision 152-D be contributed to superannuation if the person is under preservation age;
- capital *proceeds* from the disposal of assets that qualify for the CGT exemption in Subdivision 152-B ***[Schedule 1, item 1, subsection 292-100(2)]***; and
- capital *proceeds* from the disposal of assets that would have qualified for the CGT exemption in Subdivision 152-B but for:
  - the disposal of the asset resulting in no capital gain or a capital loss ***[Schedule 1, item 1, subsection 292-100(2)]***;

- the asset being a pre-CGT asset ***[Schedule 1, item 1, subsection 292-100(5)]***; or
- the asset being disposed of before the required 15-year holding period had elapsed because of the permanent incapacity of the person (which occurred after the asset was purchased) ***[Schedule 1, item 1, subsections 292-100(3) and (6)].***

1.100 This exemption recognises that many small business people invest in their business rather than make regular contributions into superannuation and later use the equity in their business to fund their retirement.

1.101 A person's CGT cap is reduced by the amount of each contribution they elect to be covered by the exemption from the non-concessional contributions cap. This includes elections made for contributions made between 10 May 2006 and 30 June 2007 (the deemed 2006-07 year). ***[Schedule 1, item 1, subsection 292-105(2) and Schedule 1, item 25, paragraph 292-80(3)(h) of the Income Tax (Transitional Provisions) Act 1997]***

1.102 A contribution will only count towards the CGT cap if the person notifies their superannuation provider before, or when, the contribution is made. This will ensure that the superannuation provider is able to accept the contribution and that it is not reported against the non-concessional contributions cap but is instead reported correctly against the CGT cap. It also provides the person with the choice as to whether all or part of a contribution uses their non-concessional contributions cap or their CGT cap. ***[Schedule 1, item 1, subsection 292-100(9)]***

1.103 Where the person has the CGT event, the contribution must be made no later than the day the person is required to lodge their tax return for the financial year in which the CGT event occurred or 30 days after the day the person received the capital proceeds, whichever is later. Where the capital proceeds are received and contributed in instalments, each instalment is a separate contribution which must be made within the above timeframes. ***[Schedule 1, item 1, paragraphs 292-100(2)(b) and (7)(b)]***

1.104 A CGT concession stakeholder of an entity that had a capital gain disregarded under Subdivision 152-B (or would have if certain conditions were met) is also entitled to use the CGT cap in

the above circumstances. However, the entity must make a payment to that person within two years of the CGT event and that person must make a contribution within 30 days of that payment for the contribution to qualify for the CGT cap. The amount of the contribution is limited to the person's stakeholder's control percentage of the capital proceeds up to the CGT cap amount. ***[Schedule 1, item 1, subsection 292-100(4)]***

1.105 A CGT concession stakeholder of an entity that had a capital gain disregarded under Subdivision 152-D is also entitled to use the CGT cap in the above circumstances. However, the entity must make a payment to that person that satisfies the conditions in section 152-325. Subject to meeting those conditions, the contribution must be made within 30 days of that payment for the contribution to qualify for the CGT cap. The amount of the contribution can be no more than the capital gain and can not exceed the amount of this payment from the entity. ***[Schedule 1, item 1, subsection 292-100(8)]***

Example 1.9

Ruth, aged 59, sells an active asset used in her small business which she has owned continuously for over 15 years. The proceeds from the sale are $1.1 million. She qualifies for the CGT exemption in Subdivision 152-B and disregards the capital gain of $390,000 on this basis. Ruth would like to contribute the entire proceeds to her superannuation fund.

Assuming Ruth has not previously made any contributions or used her CGT cap, she may elect to contribute $1 million under the cap exemption and have the remaining $100,000 count towards her non-concessional contributions cap. This would allow her to make an additional $50,000 worth of non-concessional contributions in the year without exceeding her annual cap.

Alternatively, as she is under 65, she may use the bring forward to contribute $450,000 and only use her CGT cap for the remaining $650,000. This will leave Ruth with a CGT cap of $350,000 for use in the future. However, any further non-concessional contributions made in that year, and the following two years, will exceed her non-concessional contributions cap and result in an excess contributions tax liability.

Note that if Ruth had her capital gain disregarded under the Subdivision 152-D exemption instead she would have only been

able to contribute the capital gain (ie, up to $390,000) and not the capital proceeds under the cap exemption.

Transitional arrangements for the non-concessional contributions cap

Application of the non-concessional contributions cap between 10 May 2006 and 30 June 2007 — the deemed 2006-07 financial year

1.106 All individuals who are eligible to contribute (eg, those aged 65 to 74 must satisfy the work test set out in the *Superannuation Industry (Supervision) Regulations 1994*) will have a cap of $1 million for non-concessional contributions between 10 May 2006 and 30 June 2007. This period will be treated as the 2006-07 financial year for the purposes of the cap. ***[Schedule 1, item 25, subsection 292-80(1) and paragraph 292-80(3)(c) of the Income Tax (Transitional Provisions) Act 1997]***

1.107 Excess non-concessional contributions tax and the associated administration arrangements will apply with the following modifications:

- the bring forward arrangements will not apply until 1 July 2007 ***[Schedule 1, item 25, paragraph 292-80(3)(d) of the Income Tax (Transitional Provisions) Act 1997]***;
- contributions in excess of a person's age-based deduction limit will be counted as a non-concessional contribution (as these contributions are undeducted employer contributions) ***[Schedule 1, item 25, subsections 292-80(5) and (6) of the Income Tax (Transitional Provisions) Act 1997)]***;
- the person's CGT cap amount will be $1 million at 10 May 2006 and any contributions made during this period will reduce their CGT cap from 1 July 2007 ***[Schedule 1, item 25, paragraphs 292-80(3)(e) and (3)(h) of the Income Tax (Transitional Provisions) Act 1997]***; and
- the choice to use the personal injury or CGT cap exemption from the non-concessional contributions cap must be given to the superannuation provider by 31 July 2007 ***[Schedule 1, item 25, paragraphs 292-80(3)(f) and (g) of the Income Tax (Transitional Provisions) Act 1997]***.

Transitional release authorities

1.108 A person who has non-concessional contributions in excess of $1 million for the period 10 May 2006 to 6 December 2006 can apply to the Commissioner for a transitional release authority. This application *must* be made before 1 July 2007. ***[Schedule 1, item 25, section 292-80A of the Income Tax (Transitional Provisions) Act 1997]***

1.109 The transitional release authority may be given to a superannuation provider within 21 days of receipt and authorises the person's superannuation provider to release the amount of the excess non-concessional contributions. ***[Schedule 1, item 25, section 292-80B of the Income Tax (Transitional Provisions) Act 1997]***

1.110 The superannuation provider must pay the amount to the person within 30 days of receipt. A superannuation provider will be required to give to the Commissioner a statement under section 390-65 of the *Taxation Administration Act 1953* (TAA 1953) in relation to this payment. ***[Schedule 1, item 25, paragraph 292-80(2)(c) of the Income Tax (Transitional Provisions) Act 1997]***

1.111 If a transitional release authority is given to a superannuation provider, and an amount is released, the person's non-concessional contributions for the year will be reduced by any amounts returned to them. These amounts are non-assessable, non-exempt income to the extent they do not exceed the total amount that is authorised for release. ***[Schedule 1, item 25, paragraph 292-80(3)(i) of the Income Tax (Transitional Provisions) Act 1997 and item 1, subsections 304-15(2) and (3)]***

1.112 Where a person accesses more than the amount authorised for release, that amount will be included in their assessable income and subject to income tax at marginal rates. In addition, they will be liable for an administrative penalty. ***[Schedule 1, item 1, subsection 304-15(4) and item 23, section 288-100 of the TAA 1953]***

1.113 If a transitional release authority is not actioned, and the excess contributions are not removed from the superannuation system, those contributions will continue to be included in the calculation of a person's excess non-concessional contributions tax liability for the year. ***[Schedule 1, item 25, paragraph 292-80(3)(i) of the Income Tax (Transitional Provisions) Act 1997]***

Example 1.10

Pat makes a contribution of $1.3 million on 11 May 2006. Not wanting to breach the cap on non-concessional contributions he applies to the Commissioner for a transitional release authority on 3 May 2007. The Commissioner issues the transitional release authority for $300,000 on 2 June 2007.

Pat gives the transitional release authority to his superannuation provider within 21 days. His fund is obligated to return the excess to him within 30 days. Pat's non-concessional contributions for the year will be reduced by the amounts returned to him by his fund under the transitional release authority.

Commissioner's discretion to disregard or reallocate contributions

1.114 A person can apply to the Commissioner for a written determination that, for the purposes of working out their excess contributions for a financial year, all or part of the contributions should be either disregarded or allocated to another financial year. ***[Schedule 1, item 1, subsection 292-465(1)]***

1.115 A person must request the exercise of the discretion within 60 days of receiving an excess contributions tax assessment, although a longer period may be allowed by the Commissioner. ***[Schedule 1, item 1, subsection 292-465(2)]***

1.116 The Commissioner may make the determination only if he or she considers that there are special circumstances and making the determination is consistent with the object of Division 292. ***[Schedule 1, item 1, subsection 292-465(3)]***

1.117 The courts have considered what 'special circumstances' means in many different contexts. It is clear from the case law that special circumstances are unusual circumstances, or circumstances out of the ordinary. Whether circumstances are special will vary from case-to-case as the context requires, but in this context they must make it unjust, unreasonable or inappropriate to impose the liability for excess contributions tax.

1.118 However, in making the determination, the Commissioner may have regard to certain matters specified in the law. These are whether:

- the contributions made in a particular financial year would be allocated more appropriately to another year; and
- it was reasonably foreseeable a particular contribution would result in a person having an excess contribution when the contribution was made.

[Schedule 1, item 1, subsections 292-465(5) and (6)]

1.119 When considering whether an excess is reasonably foreseeable, the Commissioner may consider the terms of any agreement or arrangement between the individual and another person where those terms affect the amount or timing of the contribution. For example, where contributions are made by an employer under a workplace agreement, industrial award or an effective salary sacrifice agreement the Commissioner will need to consider the terms of those agreements. The Commissioner may also consider the extent to which the individual has control over the making of the contribution. For example, a person who is making a contribution towards the end of a financial year should ensure that the fund receives the contribution before the end of the financial year to ensure it is taken into account in that year and not the subsequent one. ***[Schedule 1, item 1, subsection 292-465(4)]***

1.120 If the Commissioner determines that contributions can be disregarded or reallocated, for the purposes of working out a person's excess contributions for a financial year, the Commissioner must give the person a copy of the determination. ***[Schedule 1, item 1, subsection 292-465(7)]***

1.121 The Commissioner may exercise the discretion in relation to any assessment made for a financial year commencing after 30 June 2007. He or she may also exercise the discretion in relation to an assessment made under the special transitional rules that apply to the period from 10 May 2006 to 30 June 2007. ***[Schedule 1, item 25, subsection 292-80(2) of the Income Tax (Transitional Provisions) Act 1997)]***

Example 1.11

Barbara has entered into an effective salary sacrifice arrangement with her employer to sacrifice 20 per cent of her salary into superannuation. This results in a contribution of $45,000 for the year. However, during the same year, the ATO collects an SG charge from Barbara's previous employer for quarters in an earlier financial year and pays $20,000 to her superannuation fund. As a result, Barbara's fund reports to the ATO $65,000 in concessional contributions for the financial year.

Barbara is issued a concessional contributions tax assessment for an excess of $15,000. Barbara applies to the Commissioner to use his discretion. The Commissioner may exercise his discretion as $20,000 of her concessional contributions are properly referrable to a previous financial year. It may be unreasonable to assess Barbara to the excess contributions tax where it is clear that but for her previous employer's failure to provide superannuation support to Barbara in a timely way, Barbara would not have had excess concessional contributions for the year. If the discretion is exercised, Barbara's concessional contributions for the year would be reduced to $45,000. The Commissioner may also reallocate the $20,000 concessional contributions to Barbara's concessional contributions for the previous year.

Example 1.12

Jaylee is 63 and makes a $750,000 contribution to superannuation in the 2009-10 financial year, for which she cannot claim a deduction. After receiving an excess non-concessional contributions tax assessment, Jaylee applies for the Commissioner to exercise his discretion to re-allocate $300,000 of the contributions to earlier financial years in which she did not make contributions, arguing that they should be counted under the bring forward provisions.

The Commissioner will not exercise the discretion in this case as Jaylee's circumstances are not exceptional and the outcome would not be consistent with the object of the Division.
The contributions caps operate on a 'use it or lose it' basis. That is, non-concessional contributions are subject to annual limits with the ability for those under age 65 to bring forward future entitlements to two years worth of non-concessional contributions. Past years' entitlements can not be carried forward in this manner.

Example 1.13

George's employer contributes $50,000 each year to his superannuation plan under the terms of an effective salary sacrifice agreement. However, his employer's contribution for Year 1 was made on 3 July of Year 2. The employer's contribution for Year 2 was then made on 29 June of that same year (again during Year 2). This resulted in George having no concessional contributions in Year 1 but concessional contributions of $100,000 in Year 2.

The Commissioner may exercise his discretion in this case, to allocate $50,000 to Year 1 as the first contribution is more appropriately allocated to Year 1. Reallocating the amount to Year 1 would be consistent with the object of the excess contributions taxes and fairly matches the employer's contributions to the financial year in which they should have been made to George's fund.

Example 1.14

Antoni is a member of an employer sponsored superannuation plan. Under the terms of the plan Antoni is required to contribute 5 per cent of his salary ($5,000) to the fund each year. Each of his contributions will be a non-concessional contribution. However, in one particular year, Antoni also contributes $450,000 from an inheritance. Antoni is subsequently issued a tax assessment for his excess non-concessional contributions of $5,000. Antoni applies to the Commissioner for an exercise of the discretion.

The Commissioner may decide not to exercise his discretion in this case, as it was reasonably foreseeable that Antoni would exceed his non-concessional contribution cap in that year as a result of making a contribution of $450,000.

Example 1.15

Helen instructs her overseas superannuation provider to pay an amount to her Australian superannuation provider on 15 August 2007. At the time of giving her instructions Helen tried to specify an amount in the foreign currency that would not exceed $450,000, taking into account the prevailing exchange rate. However, the amount actually paid on 19 August 2007 was $454,500, the exchange rate having changed more than she expected.

The Commissioner may exercise his discretion and disregard the amount of $4,500. It was not reasonably foreseeable that Helen would exceed her non-concessional contribution cap for that year and it may be unjust to impose the tax in circumstances in which Helen attempted to contribute an amount less than the non-concessional contributions cap.

Release authorities

1.122 Generally, the superannuation preservation rules restrict the ability of individuals to withdraw money from superannuation until after they have attained preservation age, and retired.

1.123 However, from 1 July 2007, where an excess contributions tax liability arises, the individual will be able to, and in some cases *must*, withdraw an amount equal to their tax liability from their superannuation provider.

1.124 The Commissioner will provide individuals liable for excess contributions tax with a release authority, that is, a written notice authorising an individual to withdraw money from a superannuation fund provider. Separate release authorities will be issued for each of the taxes (where applicable) as different arrangements apply. ***[Schedule 1, item 1, section 292-405]***

1.125 Release authorities can be presented to any of a person's superannuation providers, other than those that only hold a defined benefit interest for the individual. ***[Schedule 1, item 1, subsection 292-410(1)]***

1.126 The amount a superannuation provider is required to release is the lesser of:

- the amount specified by the person;
- the amount of excess contributions tax stated on the release authority; or
- the sum of the values of every superannuation interest (other than a defined benefit interest) held for the person.

[Schedule 1, item 1, subsections 292-415(1) and (2)]

1.127 Superannuation providers will be required to pay the amount within 30 days. These amounts are non-assessable,

non-exempt income to the extent they do not exceed the total amount that is authorised for release. ***[Schedule 1, item 1, subsections 292-415(1), 304-15(2) and (3)]***

1.128 A person can direct their superannuation provider to release money either to themselves or directly to the ATO. Payments made directly to the ATO by a superannuation provider are taken to be made in satisfaction of the person's excess contributions tax liability. ***[Schedule 1, item 1, subsection 292-415(3)]***

1.129 The proportioning rule does not apply to amounts paid under a release authority. ***[Schedule 1, item 1, subsection 292-415(5)]***

1.130 Where a person accesses more than the amount authorised for release, that amount will be included in their assessable income and subject to income tax at marginal rates. In addition, they will be liable for an administrative penalty. ***[Schedule 1, item 1, subsection 304-15(4)]***

Excess concessional contributions

1.131 Individuals will have a choice as to whether or not to withdraw the amount equal to all, or part, of their excess concessional contributions tax liability from superannuation. ***[Schedule 1, item 1, subsection 292-410(1)]***

1.132 A release authority for excess concessional contributions will expire after 90 days. The time limit on providing release authorities for excess concessional contributions tax is necessary to maintain the integrity of the superannuation preservation rules. ***[Schedule 1, item 1, subsection 292-410(1)]***

Excess non-concessional contributions

1.133 Individuals *must* withdraw the amount equal to their excess non-concessional contributions tax liability from superannuation by providing the release authority to their superannuation provider/s within 21 days. Individuals who fail to comply with this requirement will be liable for an administrative penalty. ***[Schedule 1, item 1, subsection 292-410(2) and item 23, section 288-90 of the TAA 1953]***

1.134 Where a person fails to withdraw the required amount, the Commissioner is able to present release authorities directly to superannuation providers on behalf of that person. ***[Schedule 1, item 1, subsections 292-410(3) and (4)]***

1.135 Excess contributions tax may be offset or added to other income tax debits or credits of the individual. However, a person will still be required to withdraw the amount equal to their excess non-concessional contributions tax liability from superannuation. That is, they can not withdraw the net tax liability owing where this differs from their excess non-concessional contributions tax liability.

Penalties

On the individual

1.136 An individual will be liable for an administrative penalty of 20 penalty units where:

- they fail to give a release authority for non-concessional contributions tax to a superannuation provider within 21 days after the date of the release authority ***[Schedule 1, item 23, section 288-90 of the TAA 1953]***; or

- the total amount paid by their superannuation providers exceeds the amount authorised to be released ***[Schedule 1, item 23, section 288-100 of the TAA 1953].***

Example 1.16

Shaz receives a compulsory release authority in relation to her excess non-concessional contributions tax. She presents her compulsory release authority to multiple funds and, in doing so, accesses more than the total authorised for release. Shaz will be liable for an administrative penalty.

In addition, the amount over what should have been released will be included in her assessable income in the year it was released and subject to income tax at marginal rates.

On the superannuation provider

1.137 A superannuation provider will be liable for an administrative penalty of 20 penalty units where they fail to comply with a release authority within 30 days. ***[Schedule 1, item 23, section 288-95 of the TAA 1953]***

Excess contributions tax liabilities

Assessments

1.138 The Commissioner must make an assessment of excess contributions tax if a person has excess concessional contributions or excess non-concessional contributions for a financial year. The Commissioner will not make an assessment if a person does not have excess concessional contributions or excess non-concessional contributions for a financial year. ***[Schedule 1, item 1, subsections 292-230(1) and (2)]***

1.139 The Commissioner must give the person a notice of the excess contributions tax assessment (or amended assessment) as soon as practicable. ***[Schedule 1, item 1, subsections 292-230(3) and 310(2)]***

1.140 Excess contributions tax assessments may be issued by the Commissioner as part of an individual's income tax assessment notice, or any other assessment notice. ***[Schedule 1, item 1, subsections 292-230(4) and 310(3)]***

1.141 Consistent with the arrangements applying to an individual's other income tax liabilities, excess contributions tax will be payable 21 days after the Commissioner has given the person the notice of assessment. Amounts that remain unpaid after that period will attract the general interest charge (GIC). The Commissioner may remit the GIC under existing remission guidelines. ***[Schedule 1, item 1, sections 292-385 and 292-390]***

1.142 The Commissioner may issue a part-year assessment and treat the period as if it is a financial year. This would occur in circumstances where the Commissioner is of the opinion a part-year assessment is justified. In these cases the Commissioner will also be required to make an assessment in relation to the actual financial year as soon as possible after the end of that year unless the assessment would not differ in a material way from the part-year assessment. A part-year assessment does not provide more than one cap for either the excess concessional contributions cap or the excess non-concessional contributions cap. ***[Schedule 1, item 1, section 292-235]***

1.143 The validity of assessments will not be affected through non-compliance with provisions in the ITAA 1936 and the ITAA 1997. ***[Schedule 1, item 1, section 292-240]***

1.144 Objections to assessments can be made under Part IVC of the TAA 1953. ***[Schedule 1, item 1, section 292-245]***

1.145 Evidence requirements in section 177 of the ITAA 1936 will apply to these assessments. ***[Schedule 1, item 1, section 292-250]***

1.146 The Commissioner has the same powers to obtain information as provided by section 264 of the ITAA 1936. ***[Schedule 1, item 1, section 292-470]***

1.147 The reporting obligations on superannuation providers to enable the Commissioner to make excess contributions tax assessments are contained in Division 390 in Schedule 1 to the TAA 1953.

Amended assessments

1.148 At any time up to four years after an original excess contribution tax assessment has been given to a person for a financial year the Commissioner can issue an amended excess contribution tax assessment that either increases or decreases the excess contribution tax liability. An amended assessment can be issued by the Commissioner to the person in a similar way as the original assessment. ***[Schedule 1, item 1, sections 292-305 and 292-310]***

1.149 The day on which the Commissioner first gives a notice of assessment to the person for a financial year is the original excess contribution assessment day. ***[Schedule 1, item 1, subsection 292-305(2)]***

1.150 Assessments can be amended by the Commissioner after the end of the four years of being made if an individual has requested an amendment and provided any necessary information within the four year amendment period. ***[Schedule 1, item 1, section 292-315]***

1.151 Amended assessments can only be further amended within four years of the particular amended assessment. ***[Schedule 1, item 1, section 292-325]***

1.152 The assessment can be amended at any time if the Commissioner is of the opinion that a person or provider has not given a full and true disclosure, or an under-assessment has been made and the under-assessment has been as a result of fraud or evasion. ***[Schedule 1, item 1, section 292-320]***

1.153 An assessment (or amended assessment) can be amended at any time to give effect to a review or appeal decision or to be reduced pending such a decision, or as a result of an objection if the Commissioner considers it just to do so. ***[Schedule 1, item 1, section 292-330]***

1.154 Where an amended assessment results in a refund it will be paid in accordance with the existing guidelines. ***[Schedule 1, item 1, section 292-395]***

Chapter 2
Taxation of benefit payments

Outline of chapter

2.1 Schedule 1 to this Bill establishes a new, simplified regime for the taxation of superannuation benefits. It also removes significant complexity from the taxation arrangements that apply to the payment of superannuation benefits from 1 July 2007. Under this simplified regime:

- the payment of superannuation benefits, whether in the form of a superannuation lump sum or a superannuation income stream, to persons aged 60 and over is tax free where those benefits have been subject to tax in the fund;

- where a superannuation benefit contains an amount that has not been subject to tax in the fund, it will continue to be subject to tax. However, where the benefit is paid to persons aged 60 and over, a lower rate of tax applies than currently. This is relevant generally to those people (eg, public servants), who are members of a superannuation fund established by the Australian Government or a state government;

- simplified taxation arrangements apply to the payment of superannuation benefits to persons below age 60, primarily based on the existing taxation arrangements set out in the *Income Tax Assessment Act 1936* (ITAA 1936);

- reasonable benefit limits (RBLs) are abolished; and

- some existing provisions which are retained in the simplified regime are rewritten in a simplified and modernised form to improve the readability of the law.

2.2 A higher rate of tax on transfers over $1 million from untaxed to taxed schemes is introduced separately in the

Superannuation (Excess Untaxed Roll-over Amounts Tax) Bill 2006 to ensure that each Bill deals with a separate object of taxation. In addition, the Superannuation (Departing Australia Superannuation Payments Tax) Bill 2006 replaces the *Income Tax (Superannuation Payments Withholding Tax) Act 2002* to reflect the new components of superannuation benefits while retaining the same rates of taxation.

2.3 All legislative amendments are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated.

Context of amendments

2.4 The taxation of superannuation is currently complex, with different arrangements applying to the taxation of contributions, earnings and benefits.

2.5 The report of the Taskforce on Reducing Regulatory Burdens on Business, *Rethinking Regulation* recommended that high priority be given to comprehensive simplification of the tax rules for superannuation benefits.

2.6 The taxation of superannuation benefits is determined by reference to the following factors:

- the age of the member;
- the form of the superannuation benefit, that is, whether it is a superannuation lump sum or superannuation income stream benefit; and
- the taxation arrangements that apply to each component that comprise the superannuation benefit.

2.7 A superannuation benefit may comprise up to eight different components. Each component is subject to different taxation arrangements.

2.8 Superannuation benefits are subject to RBLs that limit the amount of superannuation benefits a person may receive on a concessionally taxed basis. Amounts in excess of the RBL are subject to a higher rate of tax.

2.9 The complexity of these arrangements affects the ability of individuals to make decisions relating to their retirement and adds to the administration costs for superannuation funds.

Summary of new law

2.10 Schedule 1 establishes a new regime for the taxation of superannuation benefits in the ITAA 1997.

2.11 Schedule 1 simplifies the taxation of superannuation benefits by removing the tax payable upon a superannuation benefit where it is paid to a person aged 60 and above and the benefit has already been subject to tax on contributions and earnings. The taxation arrangements that apply to the payment of a superannuation benefit to persons below age 60 are also streamlined.

Taxation of a superannuation benefit

2.12 A superannuation benefit may comprise the following:

- a tax free component;
- a taxable component which includes:
  - an element taxed in the fund; and / or
  - an element untaxed in the fund.

2.13 The tax free component of a superannuation benefit is generally made up of contributions from a person's post-tax income and by amounts which represent the portion of a superannuation benefit that accrued before 1 July 1983.

2.14 The tax free component is, uniformly, not assessable income and not exempt income. That is, it is paid tax free.

2.15 The taxable component of a superannuation benefit is the total value of the superannuation benefit *less* the tax free component. The taxable component is usually made up of tax deductible contributions made to the superannuation fund by the person and / or by the employer on the person's behalf, as well as

earnings on all contributions. For most people the taxable component is entirely made up of an element taxed in the fund, that is, a part that has been subject to tax at the time that contributions were made and upon earnings.

2.16 In comparison, an element untaxed in the fund usually arises in public sector superannuation plans where tax has not been paid on contributions or earnings, or from unfunded schemes.

2.17 Different taxation arrangements apply to the element taxed in the fund and the element untaxed in the fund. These arrangements are summarised in Tables 2.1 and 2.2. The tax rates specified in the tables are maximum rates of tax. The Medicare levy is also payable upon any superannuation benefit where a tax rate greater than zero per cent applies.

Table 2.1: Superannuation member benefit — element taxed in the fund (a)

Age	*Superannuation lump sum*	*Superannuation income stream*
Aged 60 and above	Tax free (not assessable, not exempt income).	Tax free (not assessable, not exempt income).
Preservation age to age 59	Zero per cent tax up to low rate cap of $140,000 (indexed). Any amount above low rate cap is subject to 15 per cent tax.	Marginal tax rates and 15 per cent tax offset.
Below preservation age	Taxable component is subject to 20 per cent tax.	Marginal tax rates (no tax offset) (b).

(a) Tax free component is always tax free.

(b) A disability superannuation income stream also receives a 15 per cent offset.

Table 2.2: Superannuation member benefit — element untaxed in the fund (a)

Age	*Superannuation lump sum*	*Superannuation income stream*
Aged 60 and above	15 per cent up to the untaxed cap amount of $1 million (indexed) per superannuation plan. The top marginal rate applies to amounts above this cap.	Marginal tax rates and 10 per cent tax offset.
Preservation age to age 59	15 per cent up to the low rate cap amount of $140,000 (indexed). 30 per cent on those amounts up to the untaxed plan cap of $1 million (indexed). The top marginal tax rate applies to any amount above the untaxed plan cap.	Marginal tax rates (no tax offset).
Below preservation age	30 per cent up to untaxed plan cap of $1 million (indexed). The top marginal rate applies to amounts above this cap.	Marginal tax rates (no tax offset).

(a) Tax free component is always tax free.

Disability benefit

2.18 Where a person receives a disability superannuation income stream before reaching his or her preservation age, he or she is entitled to claim a 15 per cent tax offset in respect of the element taxed in the fund.

Superannuation death benefit

2.19 Where a person dies, his or her superannuation benefit may be paid to another person (or to the trustee of a deceased estate). This person may be a dependant or a non-dependant of the deceased person for tax purposes. For tax purposes, a dependant may include any spouse or former spouse of the deceased, his or

her children under the age of 18 and any other person who was dependant upon the deceased.

2.20 Different taxation arrangements apply to the payment of a superannuation death benefit to a person that is a dependant of the deceased person for tax purposes in comparison to a person that is not a dependant of the deceased for tax purposes. The taxation arrangements also differ depending on whether the amount is paid as a lump sum or an income stream and, in the case of an income stream, the age of the deceased person and the recipient.

2.21 From 1 July 2007, a person who is not a dependant of the deceased will not be able to receive a superannuation income stream under amendments to be made to the *Superannuation Industry Supervision Regulations 1994*. Non-dependants for whom a death benefit superannuation income stream commenced prior to 1 July 2007 will be taxed in the same manner as dependants.

2.22 Tables 2.3 and 2.4 summarise the taxation arrangements that apply to the payment of a superannuation death benefit from 1 July 2007. The tax rates specified in the tables are maximum rates of tax. The Medicare levy is also payable upon any superannuation benefit where a tax rate greater than zero per cent applies.

Table 2.3: Superannuation death benefits paid to a dependant (a)

Age of deceased	*Superannuation death benefit*	*Age of recipient*	*Taxation*
Any age	Lump sum	Any age	Tax free (not assessable, not exempt income).
Aged 60 and above	Income stream	Any age	Taxable component — element taxed in the fund is tax free (not assessable, not exempt income). Taxable component — element untaxed in the fund is subject to marginal tax rates and the person is entitled to a 10 per cent tax offset upon this amount.
Below age 60	Income stream	Above age 60	Taxable component — element taxed in the fund is tax free (not assessable, not exempt income). Taxable component — element untaxed in the fund is subject to marginal tax rates and the person is entitled to a 10 per cent tax offset upon this amount.
		Below age 60	Taxable component — element taxed in the fund is subject to marginal tax rates and the person is entitled to a 15 per cent tax offset upon this amount. Taxable component — element untaxed in the fund is subject to marginal tax rates.

(a) Tax free component is always tax free.

Table 2.4: Superannuation death benefits paid to a non-dependant (a)

Age of deceased	*Superannuation death benefit*	*Age of recipient*	*Taxation*
Any age	Lump sum	Any age	Taxable component — element taxed in the fund is subject to 15 per cent tax. Taxable component — element untaxed in the fund is subject to 30 per cent tax.
Any age	Income stream	Any age	Not applicable. Income streams that had commenced prior to 1 July 2007 will be taxed as if received by a dependant.

(a) Tax free component is always tax free.

Supporting Bills

2.23 A higher rate of tax on transfers over $1 million from untaxed to taxed schemes is introduced separately by the Superannuation (Excess Untaxed Roll-over Amounts Tax) Bill 2006 to ensure each Bill deals with a separate object of taxation. The Superannuation (Departing Australia Superannuation Payments Tax) Bill 2006 replaces the *Income Tax (Superannuation Payments Withholding Tax) Act 2002* to reflect the new components of superannuation benefits while retaining the same rates of taxation.

2.24 The taxation of certain other amounts at the top marginal tax rate will be achieved by consequential amendments that will be made to the *Income Tax Rates Act 1986*.

Comparison of key features of new law and current law

New law	*Current law*
Taxation of benefit payments	
Superannuation benefits which have been subject to tax on contributions and earnings are tax free for all people aged 60 and over from 1 July 2007.	Superannuation lump sum benefits paid from a taxed source comprise up to eight different components that are each subject to different taxation arrangements. Five per cent of the pre-July 1983 component is subject to marginal tax rates. Five per cent of the concessional component is subject to marginal tax rates. All undeducted contributions, post-June 1994 invalidity payments and capital gains tax exempt components are tax free. The non-qualifying component is subject to marginal tax rates. The excessive component is subject to 38 per cent tax. Superannuation income stream benefits paid from a taxed source are included in assessable income with a 15 per cent tax offset applying after age 55.
Element untaxed in the fund	
Where a person aged 60 and over receives a superannuation income stream that contains an element untaxed in the fund (ie, no contributions or earnings tax has been paid on this element), he or she is entitled to a 10 per cent tax offset upon this amount. Where a person aged 60 and over receives a superannuation lump sum that contains an element untaxed in the fund, a 15 per cent tax is imposed on the element untaxed in the fund up to the	Where a person aged 55 and over receives a superannuation income stream that contains an element untaxed in the fund, this amount is included as part of the person's assessable income and subject to marginal tax rates. Where a person aged 55 and over receives a superannuation lump sum that contains a post-June 1983 untaxed element, this amount is subject to 15 per cent tax up to a low rate threshold ($135,590 in 2006-07). Amounts

New law	*Current law*
untaxed plan cap of $1 million (indexed) and the top marginal tax rate applies to amounts above this cap.	above this amount are subject to 30 per cent tax and amounts above the RBL are subject to the top marginal tax rate.
Reasonable benefit limits	
RBLs are abolished.	The RBL system determines the maximum amount of superannuation benefits that a person may receive during his or her lifetime on a concessionally taxed basis. Where a superannuation lump sum or superannuation income stream exceeds the lump sum RBL or pension RBL, excess amounts are taxed at a higher rate.
Superannuation death benefits	
A lump sum death benefit paid to a dependant is tax free. A lump sum death benefit paid to a non-dependant is taxed at 15 per cent (element taxed in the fund) or 30 per cent (element untaxed in the fund). A superannuation income stream death benefit is tax free (element taxed in the fund) or taxed at marginal rates less a 10 per cent tax offset (element untaxed in the fund) if either the deceased or recipient is over the age of 60. All other superannuation income stream death benefits are taxed at marginal rates and receive a 15 per cent offset (element taxed in the fund) or no offset (element untaxed in the fund).	A lump sum death benefit paid to a dependant is tax free up to the deceased's pension RBL. A lump sum death benefit paid to a non-dependant is taxed at 15 per cent (element taxed in the fund) or 30 per cent (element untaxed in the fund) up to the deceased's pension RBL. A superannuation income stream death benefit is taxed at marginal rates and receives the same rebate as the original pension (if any).

Detailed explanation of new law

Overall structure

2.25 The structure of this Division is based on the following outline, and addresses 'superannuation member benefits' (including 'superannuation lump sums' and 'superannuation income streams') from 'complying superannuation plans', 'superannuation death benefits', 'superannuation benefits' paid from 'non-complying superannuation plans', 'roll-overs' and key concepts that are used throughout this Bill.

Division 301	Superannuation member benefits paid from a complying plan
Subdivision 301-B	Member benefits: general rules
Subdivision 301-C	Member benefits: elements untaxed in the fund
Subdivision 301-D	Departing Australia superannuation payments
Subdivision 301-E	Superannuation lump sum member payments less than $200
Division 302	Superannuation death benefits paid from a complying plan
Subdivision 302-B	Death benefits to dependants
Subdivision 302-C	Death benefits to non-dependants
Subdivision 302-D	Definitions relating to dependants
Division 303	Superannuation benefits paid in special circumstances
Division 304	Superannuation benefits in breach of statutory requirements
Division 305	Superannuation benefits from non-complying superannuation plans
Subdivision 305-A	Superannuation benefits paid from resident non-complying superannuation plans
Subdivision 305-B	Superannuation benefits paid from foreign superannuation funds
Division 306	Roll-overs
Division 307	Key concepts
Subdivision 307-A	Superannuation benefits generally
Subdivision 307-B	Superannuation lump sums and income streams
Subdivision 307-C	Components of superannuation benefit
Subdivision 307-D	Superannuation interests

Subdivision 307-E	Elements taxed and untaxed in the fund of the taxable component of a superannuation benefit
Subdivision 307-F	Low rate cap and untaxed plan cap
Subdivision 307-G	Other concepts

Superannuation member benefits paid from complying plans

2.26 Division 301 sets out the taxation arrangements that apply to superannuation 'member benefits' paid from a complying superannuation plan. Member benefits are broadly all superannuation benefits other than benefits paid after the death of the member.

2.27 The tax arrangements differ in accordance with the age of the person that receives the superannuation benefit and whether the superannuation benefit is a superannuation lump sum or a superannuation income stream. It is also relevant to consider whether the 'taxable component' of the superannuation benefit includes an 'element taxed in the fund' and / or an 'element untaxed in the fund'. The Division also sets out taxation arrangements that apply to 'departing Australia superannuation payments' and certain superannuation lump sum member benefit payments that are less than $200. ***[Schedule 1, item 1, section 301-5]***

2.28 Superannuation death benefits are taxed under separate arrangements and are dealt with in paragraphs 2.68 to 2.80 of this chapter.

Member benefits: general rules

2.29 Subdivision 301-B sets out the tax treatment of the most common superannuation benefits, that is, benefits which do not include an element untaxed in the fund.

2.30 A superannuation benefit paid to a person aged 60 and over as a superannuation lump sum or superannuation income stream benefit is not assessable income and is not exempt income. 'Non-assessable non-exempt income' is defined under section 6-23 of the ITAA 1997 and it means that the person does not have to pay income tax on it — in simple terms it is tax free. ***[Schedule 1, item 1, section 301-10]***

2.31 If the superannuation benefit includes an element untaxed in the fund, this Subdivision must be read with Subdivision 301-C. Elements untaxed in the fund generally only apply to members of public sector superannuation plans.

Member benefits: person below age 60 and above preservation age

2.32 The 'tax free component' of a superannuation member benefit paid to a person who has reached his or her preservation age and is below age 60 is not assessable income and is not exempt income. The superannuation benefit may be a superannuation lump sum or superannuation income stream benefit. A person's preservation age depends on his or her birth date and is determined in accordance with Regulation 6.01 of the *Superannuation Industry (Supervision) Regulations 1994*. ***[Schedule 1, item 1, section 301-15]***

2.33 The taxable component of a superannuation lump sum benefit paid to a person who has reached his or her preservation age and is below age 60 is assessable income. The element taxed in the fund and the element untaxed in the fund combine to form the taxable component; however, each element is subject to different income tax treatment. ***[Schedule 1, item 1, section 302-20]***

2.34 Different income tax rates are payable on the element taxed in the fund of a superannuation lump sum. Up to a certain threshold, known as the 'low rate cap' amount, an offset applies which ensures that the tax rate on the element taxed in the fund does not exceed zero per cent. Any amount greater than the low rate cap amount is subject to income tax at a maximum rate of 15 per cent. ***[Schedule 1, item 1, section 301-20]***

2.35 Different taxation arrangements, outlined under paragraphs 2.46 to 2.55, apply where the taxable component of a superannuation benefit contains an element untaxed in the fund.

2.36 Both the element taxed in the fund and the element untaxed in the fund (if any) can utilise the low rate cap amount. The low rate cap amount is calculated in accordance with section 307-345 and is $140,000 for 2007-08 and indexed thereafter.

Example 2.1

Michelle received two superannuation lump sum benefits from two different superannuation plans at age 58. The first superannuation lump sum benefit amount was $150,000. The tax free component was $40,000, the taxable component included an element taxed in the fund of $60,000 and an element untaxed in the fund of $50,000. Her second superannuation lump sum was for $600,000; the tax free component was $250,000 and the taxable component (which was completely comprised of an element taxed in the fund) was $350,000.

The low rate cap amount applies first to elements taxed in the superannuation fund received in an income year. Michelle therefore did not pay tax on $140,000 of the element taxed in the fund of the two superannuation lump sum benefits.

Michelle paid a maximum 30 per cent tax (plus the Medicare levy) on the element untaxed in the fund of $50,000 and a maximum 15 per cent tax (plus the Medicare levy) on the remaining element taxed in the fund.

2.37 The taxable component of a superannuation income stream benefit paid to a person who has reached his or her preservation age and is below age 60 is assessable income. He or she is entitled to a tax offset equal to 15 per cent of the taxable component of the superannuation income stream benefit. Different taxation arrangements apply to an element untaxed in the fund that forms part of the taxable component under Subdivision 301-C. ***[Schedule 1, item 1, section 301-25]***

Member benefits — recipient under preservation age

2.38 The tax free component of a superannuation member benefit, whether a superannuation lump sum or superannuation income stream benefit, is not assessable income and not exempt income where it is paid to a person below his or her preservation age. ***[Schedule 1, item 1, section 301-30]***

2.39 The taxable component of a superannuation lump sum paid to a person below his or her preservation age is assessable income. The person is entitled to a tax offset so that the income tax payable on the element taxed in the fund of the lump sum is not greater than 20 per cent. The taxable component may include an

element untaxed in the fund and the taxation of this element is addressed under Subdivision 301-B. ***[Schedule 1, item 1, section 302-35]***

2.40 The taxable component of a superannuation income stream is assessable income where it is paid to a person who is below his or her preservation age. ***[Schedule 1, item 1, subsection 302-40(1)]***

Disability superannuation benefits

2.41 A person receives a ***disability superannuation benefit*** if he or she has suffered physical or mental ill-health and two legally qualified medical practitioners certify that the person is unlikely to be gainfully employed again in a position for which he or she is reasonably qualified, due to his or her education, experience or training. ***[Schedule 10, item 19]***

2.42 A person is ***gainfully employed*** where he or she is employed or self-employed for gain in a business, trade, profession, vocation, calling, occupation or employment. This definition extends access to disability superannuation benefits to the self-employed. ***[Schedule 10, item 36]***

2.43 Where a person receives a disability superannuation benefit, he or she is entitled to a 15 per cent tax offset on the taxable component if it is paid as a superannuation income stream. If the person receives the disability superannuation benefit as a lump sum, the tax free component of the benefit is increased to broadly reflect the period where they would have expected to have been gainfully employed. ***[Schedule 1, item 1, subsection 301-40(2) and section 307-145]***

Application of the tax offset

2.44 Sections 301-20, 301-35, 301-95, 301-105 and 301-115 set out different tax offsets that apply to the taxable component of a superannuation lump sum benefit in accordance with the age of the member and the elements of the component. These tax offsets reduce the amount of tax payable on the benefit. In practice, these sections specify the maximum income tax rates applicable to the element(s) that form part, or all, of the taxable component. Where a person would be subject to a lower rate of tax than the maximum rate specified by the offset in the relevant section, the lower rate applies.

2.45 Sections 301-25, 301-40 and 301-100 set out different tax offsets that apply to the taxable component of a superannuation income stream benefit in accordance with the age of the member. These tax offsets reduce the amount of tax payable on the benefit.

Member benefits: element untaxed in the fund

2.46 Where the taxable component of a superannuation benefit is wholly or partly made up of an element untaxed in the fund, the tax free component, and that part of the taxable component comprising an element taxed in the fund, if any, are treated on the same basis as outlined above. The taxation arrangements that apply to the tax free component and the element taxed in the fund are not affected by the taxation arrangements that apply specifically to the element untaxed in the fund. ***[Schedule 1, item 1, section 301-90]***

Member benefits (element untaxed in the fund) — recipient aged 60 or above

2.47 Where a person aged 60 or over receives a superannuation lump sum benefit that contains an element untaxed in the fund, that amount is assessable income. ***[Schedule 1, item 1, subsection 301-95(1)]***

2.48 The person is entitled to a tax offset to ensure that the tax rate that he or she is liable to pay on the element untaxed in the fund, up to the untaxed plan cap amount, is not greater than 15 per cent. Where the element untaxed in the fund is greater than this amount, the top marginal tax rate is applied in accordance with consequential amendments that will be made to the *Income Tax Rates Act 1986*. The person is entitled to a separate untaxed plan cap for each plan they receive superannuation lump sum benefits from. ***[Schedule 1, item 1, subsections 301-95(2) and (3)]***

Example 2.2

Jenny is a public servant and receives a superannuation lump sum of $500,000 at age 60. Her superannuation lump sum includes an element untaxed in the fund of $300,000, an element taxed in the fund of $100,000 and a tax free component of $100,000.

Jenny receives the element taxed in the fund and the tax free component tax free. The element untaxed in the fund is taxed at

her marginal tax rates up to a maximum rate of 15 per cent (plus the Medicare levy).

2.49 Where a person aged 60 or above receives a superannuation income stream benefit, the element untaxed in the fund is assessable income and subject to marginal tax rates. The person is also entitled to a 10 per cent tax offset on this amount. ***[Schedule 1, item 1, section 301-100]***

Example 2.3

Vern receives a superannuation income stream of $56,000 which commenced prior to 1 July 2007. The superannuation income stream has a deductible (tax free) amount of $6,000 (for contributions made from his post-tax income) and the remainder is an element untaxed in the fund.

Vern will continue to receive the deductible amount of $6,000 as the tax free component. He will also continue to be assessed on the remaining $50,000 at marginal rates, but will receive a tax offset of 10 per cent of $50,000 (ie, $5,000). The amount of tax Vern pays will therefore be reduced by up to $5,000.

Member benefits (element untaxed in the fund) — recipient aged over preservation age and below 60

2.50 Where a person who is below age 60 and has reached his or her preservation age receives a superannuation lump sum benefit, the element untaxed in the fund is assessable income and is subject to different rates of tax:

- up to the low rate cap amount (if any) — a maximum of 15 per cent;
- up to the 'untaxed plan cap' amount for each 'superannuation plan' (excluding any low rate cap amount) — a maximum of 30 per cent; and
- above the untaxed plan cap amount — the top marginal tax rate set out in the *Income Tax Rates Act 1986*.

[Schedule 1, item 1, section 301-105]

Example 2.4

> Jack is 58 years of age when he receives a superannuation lump sum of $180,000 which is completely comprised of an element untaxed in the fund. Jack has not previously received a superannuation lump sum.
>
> The amount up to Jack's low rate cap of $140,000 is taxed at his marginal tax rates up to a maximum rate of 15 per cent (plus the Medicare levy). The remaining $40,000 is taxed at Jack's marginal tax rates up to a maximum rate of 30 per cent (plus the Medicare levy).

2.51 Where a person who has reached his or her preservation age but is below age 60 commences receiving a superannuation income stream benefit, the element untaxed in the fund is assessable income and marginal tax rates apply. ***[Schedule 1, item 1, section 301-110]***

Member benefits (element untaxed in the fund) — recipient aged under preservation age

2.52 Where a superannuation lump sum benefit is paid to a person below his or her preservation age that includes an element untaxed in the fund, this amount forms part of his or her assessable income. ***[Schedule 1, item 1, subsection 301-115(1)]***

2.53 The person is entitled to a tax offset on the element untaxed in the fund up to the untaxed plan cap amount for the superannuation plan to ensure that the maximum rate of tax that can apply is 30 per cent. The top marginal tax rate applies to any amount greater than the untaxed plan cap amount, in accordance with the *Income Tax Rates Act 1986*. ***[Schedule 1, item 1, subsections 301-115(2) and (3)]***

2.54 Where a person receives more than one superannuation lump sum benefit that includes an element untaxed in the fund from two different superannuation plans, he or she is entitled to a separate untaxed plan cap in respect of each superannuation plan. ***[Schedule 1, item 1, subsection 301-115(3)]***

2.55 Where a person who is below his or her preservation age receives a superannuation income stream benefit that includes an element untaxed in the fund, this forms part of his or her assessable income and is taxed at marginal tax rates. ***[Schedule 1, item 1, section 301-120]***

Departing Australia superannuation payments

2.56 A departing Australia superannuation payment must be paid as a superannuation lump sum benefit to a person that has departed Australia. This payment must comply with one of the following:

- regulations under the *Superannuation Industry (Supervision) Act 1993* or the *Retirement Savings Account Act 1997*;
- section 67A of the *Small Superannuation Accounts Act 1995*; or
- the rules of the fund that apply to the operation of an exempt public sector superannuation scheme provided that these rules are substantially similar to the regulations set out above.

[Schedule 1, item 1, section 301-170]

2.57 Where a person receives a departing Australia superannuation payment, the benefit is not assessable and is not exempt income and, therefore, the person is not liable to pay income tax. This restates existing provisions set out in section 27GA of the ITAA 1936. ***[Schedule 1, item 1, subsection 301-175(1)]***

2.58 The benefit is however subject to a final withholding tax in accordance with the *Superannuation* (*Departing Australia Superannuation Payments Tax) Act 2006*. ***[Schedule 1, item 1, subsection 301-175(2)]***

2.59 The Superannuation (Departing Australia Superannuation Payments Tax) Bill 2006 replaces the *Income Tax (Superannuation Payments Withholding Tax) Act 2002* to reflect the new components of superannuation benefits while retaining the same rates of taxation. The rates are nil for the tax free component, 30 per cent for the element taxed in the fund and 40 per cent for the element untaxed in the fund. ***[Superannuation (Departing Australia Superannuation Payments Tax) Bill 2006]***

Superannuation lump sum member benefits less than $200

2.60 Where a person receives a member benefit that is less than $200 in value and the requirements specified in the regulations are

met, he or she receives this benefit tax free provided that it is paid as a superannuation lump sum and it is the person's entire benefit in the plan. Regulations are able to specify that this will apply to certain types of payments, for example, those relating to otherwise lost members. ***[Schedule 1, item 1, section 301-225]***

Low rate cap and untaxed plan cap amounts

Low rate cap

2.61 The low rate cap reflects the low rate threshold for eligible termination payments (ETPs) calculated under former section 159SA of the ITAA 1936. It is being retained to maintain the existing tax treatment of superannuation payments between preservation age and age 60.

2.62 The low rate cap for the 2007-08 income year is $140,000. This cap is indexed annually in accordance with section 960-285. ***[Schedule 1, item 1, section 307-345]***

2.63 As it reflects current arrangements, the low rate cap is reduced by any amount previously applied to the low rate threshold. In these cases, the first cap amount for the 2007-08 income year is calculated by adding together:

- the person's closing balance for the 2006-07 income year that is calculated in accordance with former subsection 159SF(2) of the ITAA 1936; and
- $4,410, that is, the difference between $140,000 and the upper limit for the 2006-07 income year calculated in accordance with section 159SG of the ITAA 1936.

[Schedule 1, item 25, section 307-345 of the Income Tax (Transitional Provisions) Act 1997]

2.64 The low rate cap is a lifetime limit. The low rate cap is therefore reduced by any amount for which a person has received a tax offset under subsection 301-20(4) or 301-105(4) which applies a tax offset to those payments or amounts that are counted towards the low rate cap amount. ***[Schedule 1, item 1, subsection 307-345(2)]***

Untaxed plan cap amount

2.65 The untaxed plan cap amount ensures that the concessionality of benefits that have not been subject to contributions or earnings tax in a superannuation fund is targeted appropriately. The untaxed plan cap amount is necessary as the caps that operate so as to limit the amount of superannuation contributions that a person can make (or an employer can make upon his or her behalf) do not apply to those employer contributions that are included as part of an element untaxed in the fund.

2.66 The untaxed plan cap amount for the 2007-08 income year is $1 million. This cap is indexed annually in accordance with section 960-285. ***[Schedule 1, item 1, section 307-350]***

2.67 The untaxed plan cap amount is a per plan limit, that is, a separate untaxed plan cap applies to each superannuation plan from which a person receives superannuation lump sum member benefits. The untaxed plan cap amount for each superannuation plan is reduced by the total amount of each element untaxed in the fund of a superannuation lump sum that a person has received, including roll-overs. ***[Schedule 1, item 1, subsection 307-350(2)]***

Superannuation death benefits

Superannuation death benefits paid from complying plans

2.68 Division 302 sets out the taxation arrangements that apply to the payment of 'superannuation death benefits'. These arrangements depend on whether the person that receives the superannuation death benefit is a dependant of the deceased or not and whether the amount is paid as a 'lump sum superannuation death benefit' or a 'superannuation income stream death benefit'. The current definition of a dependant for tax purposes, which includes individuals in an interdependency relationship, is being maintained. In the case of a superannuation income stream death benefit, it is also relevant to consider the age of the deceased person and the recipient. ***[Schedule 1, item 1, sections 302-5, 302-195 and 302-200]***

2.69 From 1 July 2007, a person who is not a dependant of the deceased will not be able to receive a superannuation income stream under amendments to be made to the *Superannuation*

Industry Supervision Regulations 1994. Non-dependants for whom a death benefit superannuation income stream commenced prior to 1 July 2007 will be taxed in the same manner as dependants.

Superannuation death benefits paid to a trustee of a deceased estate

2.70 A superannuation death benefit may be received by a person acting as a trustee of a deceased estate. The taxation arrangements that apply to this superannuation death benefit are determined in accordance with the taxation arrangements that would otherwise apply to the person or persons otherwise intended to benefit from the estate ***[Schedule 1, item 1, section 302-10].***

- This means that where a dependant of the deceased is expected to receive part or all of a superannuation death benefit, it will be subject to tax as if it were paid to a dependant of the deceased. However, it is also clear that the dependant is not presently entitled to this superannuation death benefit at this time and it therefore does not form part of his or her assessable income ***[Schedule 1, item 1, subsection 302-10(2)].***

- Where a person that is not a dependant is expected to receive part or all of a superannuation death benefit, it will be subject to tax as if it were paid to a non-dependant of the deceased to that extent. However, it is also clear that the non-dependant is not presently entitled to this superannuation death benefit at this time and it therefore does not form part of his or her assessable income ***[Schedule 1, item 1, subsection 302-10(3)].***

2.71 This is to ensure that the superannuation death benefit is not subject to double taxation.

Death benefits to a dependant

2.72 Where a person receives a superannuation lump sum death benefit and that person was a dependant of the deceased, it is not assessable income and is not exempt income. This means the person is not liable to pay tax on this amount. ***[Schedule 1, item 1, section 302-60]***

Superannuation income stream

2.73 A person may receive a superannuation income stream upon the death of a person upon whom he or she was dependent. This income is tax free income where the dependant is aged 60 or above or the deceased was aged 60 or above at the time when he or she died. ***[Schedule 1, item 1, section 302-65]***

2.74 Where a dependant of the deceased is under age 60 at the time he or she receives the benefit and the deceased died before he or she turned age 60:

- the tax free component of a superannuation income stream is tax free income ***[Schedule 1, item 1, section 302-70]***;
- the element taxed in the fund is assessable income and the dependant is entitled to a tax offset equal to 15 per cent of the element taxed in the fund ***[Schedule 1, item 1, section 302-75]***; and
- when the recipient turns 60 the superannuation income stream becomes tax free.

2.75 Where a child of the deceased under age 25 receives a death benefit superannuation income stream, he or she will be required to commute this benefit upon turning age 25 in accordance with payment standards prescribed under subsection 31(1) of the *Superannuation Industry Supervision Act 1993*. This commutation is treated as non-assessable and non-exempt income. ***[Schedule 1, item 1, section 303-5]***

An element untaxed in the fund

2.76 Where the taxable component of a superannuation income stream benefit includes an element untaxed in the fund, the tax free component is still tax free. Further, the person that receives the benefit is entitled to either the 15 per cent tax offset under section 302-75 or the tax free arrangements set out under section 302-65 in respect of the element taxed in the fund. The element untaxed in the fund is treated differently in accordance with section 302-80 or 302-85 depending upon the age of the deceased and the dependant. ***[Schedule 1, item 1, section 302-80]***

2.77 Where a superannuation income stream is paid to a dependant of the deceased who is age 60 or over when he or she receives the benefit or the deceased was age 60 or over at the time of his or her death, the dependant is entitled to a tax offset equal to 10 per cent of the element untaxed in the fund. ***[Schedule 1, item 1, section 302-85]***

2.78 In the event that a superannuation income stream is paid to a dependant under age 60 and the deceased died before he or she turned age 60, the element untaxed in the fund is part of the dependant's assessable income. When the dependant turns 60 they will receive a 10 per cent tax offset. ***[Schedule 1, item 1, section 302-90]***

Death benefits to a non-dependant

2.79 A non-dependant of the deceased may receive a superannuation lump sum. The tax free component of this lump sum is not assessable and is not exempt income and therefore the person is not liable to pay tax on this amount. ***[Schedule 1, item 1, section 302-140]***

2.80 Different taxation arrangements apply to the element taxed in the fund and the element untaxed in the fund that makes up the taxable component. An offset is available to ensure the tax rate on the element taxed in the fund is not greater than 15 per cent. The person is also entitled to a tax offset to ensure that the tax payable on the element untaxed in the fund does not exceed 30 per cent. ***[Schedule 1, item 1, section 302-145]***

Superannuation benefits if there is a breach of statutory requirements

2.81 The taxation arrangements set out in relation to superannuation benefits paid from a complying superannuation fund do not apply where a superannuation fund has not adhered to requirements set out in section 62 of the *Superannuation Industry Supervision Act 1993*. ***[Schedule 1, item 1, section 304-5]***

2.82 Further, these arrangements do not apply where a person receives an amount or benefit that does not meet the payment standards prescribed under subsection 31(1) or 32(1) of the *Superannuation Industry Supervision Act 1993* relating to the operation of regulated superannuation funds and regulated approved deposit funds respectively. This means that where a person receives a superannuation benefit that does not meet these

requirements, it must be included as part of his or her assessable income and is therefore subject to marginal tax rates. ***[Schedule 1, item 1, subsections 304-10(1) and (2)]***

2.83 A person must also include as part of his or her assessable income any benefit received from a retirement savings account (RSA) that is in breach of the *Retirement Savings Accounts Act 1997*, regulations made under the Act or payment standards prescribed under subsection 38(2) of the *Retirement Savings Accounts Act 1997* relating to the operating standards applying to an RSA. ***[Schedule 1, item 1, subsection 304-10(3)]***

2.84 The Commissioner of Taxation (Commissioner) retains discretion to provide that an amount may be excluded from a person's assessable income and treated as a superannuation benefit where the Commissioner is satisfied that it would be unreasonable not to do so. The Commissioner may have regard to the nature of the superannuation fund, where relevant, and any other matter that he or she may consider to be relevant. ***[Schedule 1, item 1, subsection 304-10(4)]***

2.85 Where a payment is made from a superannuation plan regarding a release authority in relation to excess contributions tax, the amount specified in the release authority is not assessable and not exempt income. Anything above this amount must be included as part of the person's assessable income in the year it is released and is subject to income tax at the person's marginal tax rates. ***[Schedule 1, item 1, section 304-15]***

Superannuation benefits paid from non-complying superannuation plans

2.86 The existing tax treatment of superannuation benefits paid from non-complying superannuation plans will be maintained, however the terminology applying to these benefits will be simplified. In summary:

- Superannuation benefits paid from 'non-complying Australian superannuation funds' are exempt income as these superannuation funds do not receive tax concessions. These funds were formerly known as eligible resident non-complying superannuation funds ***[Schedule 1, item 1, Subdivision 305-A].***

- Superannuation lump sum benefits paid from 'foreign superannuation funds' continue to be taxed on the earnings while the person was an Australian resident. These funds were formerly known as eligible non-resident non-complying superannuation funds ***[Schedule 1, item 1, Subdivision 305-B].***

- Superannuation income streams paid from foreign superannuation funds continue to be taxed at marginal rates under existing provisions set out in the ITAA 1936.

Roll-overs

2.87 Generally a 'roll-over superannuation benefit' is a lump sum superannuation member benefit that can be paid from, and to, a complying superannuation plan. It may also be paid to an entity to purchase a superannuation annuity. A person is taken to have received a roll-over superannuation benefit when a payment is made for his or her benefit or where he or she has made a direction or request that a payment be made. ***[Schedule 1, item 1, sections 306-10 and 307-15]***

2.88 Regulations may specify those superannuation benefits that are not roll-over superannuation benefits. ***[Schedule 1, item 1, paragraph 306-10(b)]***

2.89 A roll-over superannuation benefit is not assessable income and not exempt income at the time that it is made. In most

cases a roll-over superannuation benefit is not taxed at the time that the roll-over occurs. ***[Schedule 1, item 1, section 306-5]***

2.90 A person may have more than one superannuation plan with a superannuation provider. It is therefore possible that a superannuation benefit may be rolled over from one superannuation plan to another superannuation plan held by the same superannuation provider. A superannuation plan may also contain more than one superannuation interest. Therefore a superannuation interest in a superannuation plan can be paid into another superannuation interest in the same plan and qualifies as a roll-over. ***[Schedule 1, item 1, subsection 307-5(8)]***

2.91 A person may have a benefit that is a roll-over superannuation benefit that consists wholly or partly of an amount paid from an element untaxed in the fund (an untaxed roll-over amount). If the untaxed roll-over amount exceeds the person's untaxed plan cap amount for a superannuation plan tax is payable on the amount of the excess. ***[Schedule 1, item 1, section 306-15]***

2.92 The tax on the 'excess untaxed roll-over amount' is introduced under the Superannuation (Excess Untaxed Roll-over Amounts Tax) Bill 2006. ***[Schedule 1, item 1, section 306-15]***

2.93 A higher rate of tax on transfers over $1 million from untaxed plans is introduced separately in the Superannuation (Excess Untaxed Roll-over Amounts Tax) Bill 2006. The rate of tax is the top marginal tax rate plus the Medicare levy. This tax will be levied on the person on whose behalf the roll-over was made and withheld by the originating superannuation fund. ***[Superannuation (Excess Untaxed Roll-over Amounts Tax) Bill 2006]***

2.94 The Commissioner or a state or territory authority (as defined by the *Superannuation (Unclaimed Money and Lost Members) Act 1999*) may receive a superannuation benefit on behalf of a person where they cannot be found. The person is not subject to income tax on this amount as it is not assessable income and it is not exempt income. ***[Schedule 1, item 1, section 306-20]***

Key concepts

Types of superannuation benefits

What is a superannuation benefit?

2.95 Superannuation benefits are typically paid from superannuation funds, RSAs, approved deposit funds or superannuation annuities. A 'superannuation annuity' will be defined in regulations to cover superannuation income streams purchased from life insurance companies and other similar providers. ***[Schedule 1, item 1, section 307-5]***

2.96 Government agencies also make a range of payments which are superannuation benefits. These include payments by the Australian Taxation Office (ATO) as a result of the administration of the superannuation co-contribution and superannuation guarantee (SG), and payments from unclaimed money registers. ***[Schedule 1, item 1, section 307-5]***

2.97 In order to maintain the current tax treatment, the following payments are not superannuation benefits:

- Payments under an income stream because a person is temporarily unable to perform his or her normal duties as an employee. These are considered to be replacement of regular income, and are therefore taxable at marginal rates.

- Payments received from a commutation of a superannuation income stream and wholly applied to pay a superannuation contributions surcharge liability are tax free.

[Schedule 1, item 1, section 307-10]

Types of superannuation benefits

2.98 As outlined above the tax treatment of a superannuation benefit differs depending on the form in which it is paid and to whom it is paid.

2.99 A superannuation benefit can be paid as either a lump sum or as an income stream. A 'superannuation income stream'

will be defined in regulations. ***[Schedule 1, item 1, sections 307-65 and 307-70]***

2.100 A superannuation benefit can be paid as either a member superannuation benefit or a death superannuation benefit. ***[Schedule 1, item 1, section 307-5]***

2.101 A superannuation benefit is a superannuation member benefit if it is paid to the member, including if:

- the member requests that it be paid to another person or to an entity;
- it is paid as a 'contributions splitting benefit'; or
- it is paid to the member as a result of a 'family law superannuation payment'. Such payments will not be a superannuation benefit to the spouse originally entitled to the superannuation but rather will be a superannuation benefit for the receiving spouse.

[Schedule 1, item 1, subsections 307-5(5) to (7)]

2.102 A superannuation benefit is a ***superannuation death benefit*** if it is paid to you as a result of the death of another person. ***[Schedule 1, item 1, section 309-5]***

2.103 If a superannuation income stream was originally payable to the deceased, a commutation of this income stream will be a member benefit if paid after six months has passed since the person died, or three months after the will or letters of administration that relate to the person's estate has been granted probate, which ever is the later in time. This reflects existing arrangements. ***[Schedule 1, item 1, subsection 307-5(3)]***

Components of a superannuation benefit

2.104 A superannuation benefit comprises two components: the tax free component and the taxable component. ***[Schedule 1, item 1, section 307-120]***

The tax free component

2.105 The tax free component of a superannuation interest is the total value of the following segments:

- the 'contributions segment'; and
- the 'crystallised segment'.

[Schedule 1, item 1, section 307-210]

What is the contributions segment?

2.106 The contributions segment generally includes all contributions made from 1 July 2007 that have not been included in the assessable income of the superannuation provider. Typically these would be the person's non-concessional contributions. ***[Schedule 1, item 1, subsection 307-220(1)]***

2.107 Roll-over superannuation benefits (other than roll-overs from an untaxed to a taxed superannuation scheme) are not included in the assessable income of the receiving superannuation provider. The taxable component of a roll-over is therefore specifically excluded from the definition of the contributions segment. However, amounts that have been subject to excess untaxed roll-over tax are included in the contributions segment as tax has been withheld on these amounts at the top marginal tax rate (plus the Medicare levy). ***[Schedule 1, item 1, subsections 307-220(2) and (3)]***

2.108 The definition of the contributions segment also excludes a number of contributions which would otherwise have been included in a superannuation provider's assessable income, but are excluded due to the operation of other aspects of the superannuation system, such as the application of pre-1 July 1988 funding credits. ***[Schedule 1, item 1, subsection 307-220(2)]***

What is the crystallised segment?

2.109 The crystallised segment includes existing components of an interest that are being consolidated into the tax free component: undeducted contributions, the pre-July 1983 component, the capital gains tax (CGT) exempt component, the concessional component and the post-June 1994 invalidity component. The segment is calculated by assuming that an ETP representing the full value of the superannuation interest is paid just before 1 July 2007. ***[Schedule 1, item 1, section 307-225]***

2.110 The pre-July 1983 component relates to superannuation benefits accrued or accumulated before 1 July 1983. The

crystallisation of the pre-July 1983 component is discussed in further detail in paragraphs 2.140 to 2.145. ***[Schedule 1, item 1, section 307-225]***

2.111 A CGT exempt component and a post-June 1994 invalidity component would only exist if such a component had been rolled into a superannuation interest prior to 1 July 2007. The value of these components is set, or crystallised, on 30 June 2007 based on the amount of the interest attributable to that component on that date. ***[Schedule 1, item 1, section 307-225]***

2.112 Similarly, a concessional component would only exist in a superannuation interest if a redundancy, early retirement or invalidity payment that was made before 1 July 1994 was rolled over into superannuation. The value of the concessional component is set, or crystallised, on 30 June 2007 based on the amount of the interest attributable to that component on that date. ***[Schedule 1, item 1, section 307-225]***

Taxable component

2.113 The taxable component of the superannuation interest is calculated by subtracting the tax free component from the total value of the superannuation interest. The taxable component of a superannuation benefit paid from a superannuation interest consists of two elements:

- the element taxed in the fund; and / or
- the element untaxed in the fund.

[Schedule 1, item 1, section 307-215]

2.114 Consistent with the existing arrangements, the taxable component of a superannuation benefit consists of an element taxed in the fund except in a limited number of circumstances. While these provisions have been rewritten, changes only in wording or style are not intended to change the meaning of these provisions. ***[Schedule 1, item 1, section 307-275]***

2.115 The taxable component of superannuation benefits paid from untaxed superannuation schemes contain an element untaxed in the fund to the extent that no contributions and earnings tax has been paid. These schemes are generally run by the Australian

Government and the state and territory governments, generally only apply to public servants, and fall into two broad categories:

- constitutionally protected funds which are specifically exempted from tax on all contributions and earnings ***[Schedule 1, item 1, section 307-280]***; and
- superannuation funds which pay tax on contributions and earnings but are partially unfunded ***[Schedule 1, item 1, section 307-295].***

2.116 Some superannuation funds finance their benefits by making large one-off contributions. The trustee of the fund, with the consent of the contributor, can then elect for these contributions not to be taxable. Some funds also allow their members to elect whether the taxable component of their benefit is paid as an element taxed in the fund or an element untaxed in the fund. These arrangements will continue but will not be available for plans established after 5 September 2006. ***[Schedule 1, item 1, section 307-285]***

2.117 If a superannuation provider has claimed a tax deduction in respect of an insurance premium, the element untaxed in the fund of a lump sum superannuation death benefit is increased to broadly reflect the insurance component of the superannuation death benefit. The deductibility of insurance premiums broadly results in no contributions or earnings tax having been paid on this component of the superannuation death benefit. ***[Schedule 1, item 1, section 307-290]***

2.118 The taxable component of small superannuation account payments and SG payments only contain an element untaxed in the fund as these payments are made directly from the ATO and have therefore not been subject to tax in a superannuation fund. ***[Schedule 1, item 1, subsection 307-275(3)]***

Service periods

2.119 Service periods are used to calculate the pre-July 1983 amounts and adjust the tax free component of lump sum disability superannuation benefit payments and the element untaxed in the fund of superannuation death benefit payments. The definition of a 'service period' reflects the existing arrangements. ***[Schedule 1, item 1, section 307-400]***

Proportioning rule

2.120 When part of a 'superannuation interest' is paid out, the benefit will include both tax free and taxable components with the relevant portions of each reflecting the proportions such components make up of the total value of the superannuation interest. ***[Schedule 1, item 1, section 307-125]***

2.121 The proportioning rule applies to both superannuation lump sums paid after 1 July 2007 (including roll-overs) and superannuation income streams which commence after 1 July 2007. ***[Schedule 1, item 1, section 307-125]***

Step 1 — proportions of the underlying superannuation interest

2.122 The first step in applying the proportioning rule is to determine the proportion of the tax free component and the taxable component of the superannuation interest from which the superannuation benefit is being paid. ***[Schedule 1, item 1, subsection 307-125(3)]***

2.123 The tax free and taxable components of a superannuation lump sum are determined based on the value of the superannuation interest at the time just before the lump sum is paid. ***[Schedule 1, item 1, subsection 307-125(3)]***

2.124 The tax free and taxable components of a superannuation income stream are calculated based on the value of the superannuation interest at the time that the superannuation income stream is created. ***[Schedule 1, item 1, subsection 307-125(3)]***

What is the value of a superannuation interest?

2.125 The ***value*** of a superannuation interest is the total amount of all superannuation lump sums that could be paid to the person at that time. ***[Schedule 1, item 1, section 307-205]***

2.126 This general definition may not be appropriate for a minority of superannuation plans with more complex arrangements. Methods for determining the value of superannuation interests in these plans will be specified in the regulations. ***[Schedule 1, item 1, section 307-205]***

Step 2 — proportions of the superannuation benefit

2.127 These proportions must then be applied to the superannuation benefit. ***[Schedule 1, item 1, subsection 307-125(2)]***

Example 2.5

Peter is age 56 and has a superannuation interest with a value of $400,000. The interest includes a tax free component of $100,000 and a taxable component of $300,000. Peter uses all of his superannuation interest to purchase an income stream on 1 August 2007.

The tax free percentage of Peter's superannuation interest when the superannuation income stream commenced would be:

$$\frac{\text{tax free component}}{\text{value of the interest}} = \frac{\$100,000}{\$400,000} = 25\%$$

The taxable percentage of Peter's superannuation interest would therefore be 75 per cent.

Peter receives a superannuation income stream benefit of $2,000 on 1 September 2007. The tax free component of this superannuation benefit would be:

$$\$2,000 \times 25\% = \$500$$

The taxable component of this superannuation benefit would therefore be $1,500 ($2,000 – $500).

Transitional arrangements

2.128 Recipients of existing superannuation income streams as at 1 July 2007 will retain the current 'deductible amount' on their superannuation income stream unless a trigger event occurs (see paragraphs 2.131 to 2.133). The deductible amount of a superannuation income stream is currently tax free. ***[Schedule 1, item 25, section 309-37 of the Income Tax (Transitional Provisions) Act 1997]***

How are deductible amounts applied?

2.129 The amendments move the tax treatment of superannuation income stream benefits from an annual basis to a per payment basis. As a result, the annual deductible amount needs to be converted into a 'per benefit' figure to maintain the

existing tax treatment. ***[Schedule 1, item 25, subsection 309-37(2) of the Income Tax (Transitional Provisions) Act 1997)]***

2.130 This will be achieved by apportioning the annual deductible amount across each superannuation income stream according to the value of each superannuation income stream benefit received in the income year. The portion of the deductible amount applying to a particular superannuation income stream benefit will be the tax free component for that superannuation income stream benefit. ***[Schedule 1, item 25, subsection 309-37(2) of the Income Tax (Transitional Provisions) Act 1997]***

Example 2.6

Vernon is age 58 and is receiving a superannuation pension which commenced before 1 July 2007. Vernon receives monthly superannuation income stream benefits of $2,000 and his annual deductible amount is $6,000. The tax free component of the $2,000 superannuation income stream benefit is calculated as follows:

Step 1: Calculate the proportion of the superannuation income stream benefit to the benefits from that superannuation income stream received in the year:

$$\frac{\$2{,}000}{\$2{,}000 \times 12 \text{ months}} = 8.33\%$$

Step 2: Multiply the annual deductible amount by the percentage calculated in Step 1:

$$\$6{,}000 \times 8.33\% = \$500$$

The tax free component of the superannuation income stream benefit is $500. The taxable component of the superannuation income stream benefit is $1,500 ($2,000 – $500).

What are trigger events?

2.131 If the superannuation income stream does not contain an element untaxed in the fund, the proportional approach applies once the person turns age 60 or has died. The benefits become tax free in any case once the person turns age 60 or if a death benefit is paid to a dependant. As a result, this trigger event will only have a practical impact in calculating components of death benefits to

non-dependants. ***[Schedule 1, item 25, subsection 309-37(3) of the Income Tax (Transitional Provisions) Act 1997]***

2.132 In all other cases, the proportional approach does not apply unless the superannuation income stream is commuted. ***[Schedule 1, item 25, subsection 309-37(3) of the Income Tax (Transitional Provisions) Act 1997]***

2.133 Once a trigger event has occurred, the tax free amount is the sum of the unused undeducted purchase price and a pre-July 1983 amount where relevant. Both of these amounts are calculated under existing legislative provisions. The crystallisation of the pre-July 1983 component is discussed in further detail in paragraphs 2.139 to 2.144. ***[Schedule 1, item 25, subsection 309-37(4) of the Income Tax (Transitional Provisions) Act 1997]***

Application of the proportioning rule to special cases

2.134 A proportioning rule applies to family law superannuation payments under the existing arrangements so as to ensure that the various components of the superannuation interest are divided fairly between each spouse. A specific proportioning rule is no longer required as family law superannuation payments are covered by the general proportioning rule.

2.135 The proportioning rule does not affect SG payments and contributions splitting superannuation benefits (under changes that will apply from 1 July 2007) as these payments only contain a taxable component. Similarly, superannuation co-contribution payments only contain a tax free component. ***[Schedule 1, item 1, sections 307-130, 307-135 and 307-140]***

2.136 Regulations may specify an alternative method for determining the tax free and taxable components of a superannuation benefit. Alternatively, the Commissioner may either:

- make a determination, by legislative instrument, for one or more alternative methods to be used to determine those components of the benefit; or
- consent in writing to the use of another method.

[Schedule 1, item 1, subsections 307-125(4) and (5)]

2.137 In addition, regulations may specify circumstances where superannuation interests could be combined or separated and rules that determine how to allocate the tax free component, the taxable component, the element taxed in the fund and the element untaxed in the fund between superannuation interests. ***[Schedule 1, item 1, section 307-200]***

2.138 These regulations may be required to modify the application of the proportioning rule in certain circumstances, such as:

- where appropriate allowing existing arrangements which may not strictly comply with the proportioning rule to continue; and
- addressing arrangements designed to evade the proportioning rule.

Crystallising the pre-July 1983 component

2.139 Five per cent of the pre-July 1983 component is currently included in a person's assessable income and taxed at marginal rates. The 'pre-July 1983 amount' forms part of the new tax free component, and is therefore tax free for lump sums paid after 1 July 2007 (including commutations of superannuation income streams).

2.140 The mechanism for including the pre-July 1983 amount in the tax free component varies depending on the status of the superannuation interest.

2.141 For most superannuation interests, a pre-July 1983 amount will be calculated as at 30 June 2007 using the existing legislative formula. This amount will become a fixed amount and form part of the tax free component. ***[Schedule 1, item 1, section 307-225]***

2.142 Superannuation providers will have until 30 June 2008 to calculate the crystallised pre-July 1983 segment. Superannuation providers that do not calculate this amount by this date for all affected superannuation interests, are subject to an administrative penalty of 5 penalty units. ***[Schedule 1, item 23, section 288-105 of the TAA 1953]***

2.143 As outlined above, the tax free component of superannuation income streams in existence as at 1 July 2007 will be calculated based on the current 'deductible amount' concept. A pre-July 1983 amount is therefore not calculated until a trigger event occurs to move the superannuation income stream into the new arrangements.

2.144 Separate arrangements apply to superannuation benefits that have not been subject to contributions or earnings tax within the fund. This reflects existing arrangements. The pre-July 1983 segment for an element untaxed in the fund is only calculated when a lump sum superannuation benefit is withdrawn from a superannuation plan or rolled over into a taxed superannuation scheme. ***[Schedule 1, item 1, section 307-150]***

Example 2.7

Bessie has a superannuation interest of $100,000 on 30 June 2007 and a service period of 30 years (six years of which reflect pre-July 1983 service). Bessie's superannuation interest comprises a tax free component of $15,000, an element taxed in the fund of $10,000 and an element untaxed in the fund of $75,000.

The pre-July 1983 amount for Bessie's superannuation interest is calculated as at 30 June 2007 under the existing legislative formula, disregarding the value of the element untaxed in the fund:

$$(\$15,000 + \$10,000) \times \frac{6}{30} = \$5,000$$

As a result, the crystallised segment of the tax free component of Bessie's superannuation interest is increased by $5,000 and the element taxed in the fund is decreased by $5,000.

Example 2.8

Bessie subsequently makes a non-concessional contribution of $20,000 on 1 July 2007 and receives a superannuation lump sum of her entire interest of $120,000. The lump sum initially comprises a tax free component of $40,000 ($20,000 from Example 2.7 plus the non-concessional contribution of $20,000), an element taxed in the fund of $5,000 and an element untaxed in the fund of $75,000.

The pre-July 1983 amount for this lump sum is calculated by disregarding any element taxed in the fund, any crystallised segment of the tax free component and any part of the tax free component used in the earlier crystallisation. The calculation is as follows:

$$(\$20,000 + \$75,000) \times \frac{6}{30} = \$19,000$$

As a result, the tax free component of Bessie's superannuation lump sum is increased by $19,000 and the element untaxed in the fund is decreased by $19,000.

Chapter 3 Taxation of superannuation entities

Outline of chapter

3.1 Schedule 1 to this Bill incorporates the provisions of Part IX of the *Income Tax Assessment Act 1936* (ITAA 1936) that deal with the taxation of superannuation entities into the *Income Tax Assessment Act 1997* (ITAA 1997). The rewritten provisions in Division 295 of the ITAA 1997 do not change the law as it currently operates under Part IX of the ITAA 1936.

3.2 Schedule 1 also includes some new rules in relation to the taxation of superannuation entities which are a part of the *Simplified Superannuation* reforms.

3.3 This Schedule amends the ITAA 1936 to ensure that when an individual makes a tax file number (TFN) declaration in relation to a payer (their employer) the individual is also authorising their employer to provide their TFN to their superannuation fund.

3.4 This Schedule also amends the ITAA 1997 and the *Income Tax Rates Act 1986* to assess 'no-TFN contributions income', impose income tax on no-TFN contributions income, provide a particular rate of tax on that income and provide a way to refund no-TFN contributions tax when a TFN is later quoted within the required time period.

3.5 This Schedule amends the *Superannuation Industry (Supervision) Act 1993* to allow the Commissioner of Taxation (Commissioner) to regulate an employer's legal responsibilities to quote TFNs to superannuation entities.

Context of amendments

3.6 One of the main objectives of the *Simplified Superannuation* reforms is to reduce complexity in Australia's superannuation

system, which has arisen as a result of changes that have occurred over the last two decades.

3.7 Given the extent of the legislative changes to the taxation of superannuation required as a result of the *Simplified Superannuation* reforms it is appropriate that Part IX be rewritten and brought together with all other taxation of superannuation provisions in the ITAA 1997.

Summary of new law

3.8 Changes to the wording or the style used in the rewritten provisions in Division 295 do not change the law as it currently operates under Part IX of the ITAA 1936.

3.9 The provisions relating to the non-disclosure of TFNs will encourage individuals making superannuation contributions to provide their TFNs to their superannuation entities. This is required to administer the excess contributions caps as it is necessary for a member's TFN to be attached to their account. Under the current law if the individual has not provided their TFN no additional tax is levied on contributions or earnings. Accordingly many superannuation accounts and retirement savings accounts (RSAs) do not have a TFN attached. Without the new provisions relating to TFNs there is scope for abuse of the superannuation contributions cap and for people to gain unlimited access to superannuation concessions.

3.10 New provisions impose a tax on a new category of income based on superannuation contributions (where a TFN is not attached to the receiving member's account) and provide a way to have tax paid refunded to the superannuation fund or RSA provider when a TFN is later quoted within the required time period.

3.11 New provisions in the *Income Tax Rates Act 1986* provide a particular rate of tax for the tax on no-TFN contributions income which is imposed on the superannuation fund or RSA provider.

3.12 New provisions also amend the law relating to TFN declarations so that when an individual makes a TFN declaration

to their employer they are also authorising their employer to provide the TFN to their superannuation fund.

3.13 New provisions also move the regulation of an employer's responsibilities to quote an individual's TFN to their superannuation fund or RSA provider from the Australian Prudential Regulation Authority (APRA) to the Australian Taxation Office (ATO).

Comparison of key features of new law and current law

New law	*Current law*
No-TFN contributions tax	**Contributions tax**
Contributions are included in a superannuation fund or RSA provider's assessable income where a deduction is available. Where a TFN is not attached to an individual's account, deductible contributions are included in the superannuation fund or RSA provider's no-TFN contributions income. Where a TFN is subsequently provided within a four year period a superannuation fund or RSA provider is entitled to claim a tax offset for the amount of tax paid on the no-TFN contributions income.	Contributions are included in a superannuation fund or RSA provider's assessable income where a deduction is available. Contributions are taxed at the same rate irrespective of whether a TFN has been attached to the member's account.
TFN declaration form	
Individuals making a TFN declaration in relation to a payer (their employer) are taken to also provide authority for their employer to quote their TFN to the superannuation provider to which the employer makes superannuation contributions.	Individuals make a TFN declaration in relation to a payer (their employer). On that declaration individuals can also provide a separate authority for their employer to quote their TFN to the superannuation provider to which the employer makes superannuation contributions.
Employer obligations	

New law	*Current law*
No-TFN contributions tax	**Contributions tax**
The ATO is responsible for administering an employer's responsibilities to quote an individual's TFN to the superannuation fund or RSA provider under Division 1 of Part 25A of the *Superannuation Industry (Supervision) Act 1993*.	APRA is responsible for administering an employer's responsibilities to quote an individual's TFN to the superannuation fund or RSA provider under Division 1 of Part 25A of the *Superannuation Industry (Supervision) Act 1993*.

Detailed explanation of new law

Provisions rewritten and transferred from Part IX of the ITAA 1936 to Division 295 of the ITAA 1997

3.14 The rewritten provisions of Division 295 do not change the law as it currently operates under Part IX of the ITAA 1936. A finding table at the end of this chapter matches an old provision and the relevant new provision, and *vice versa*.

3.15 In the rewrite, each of the income and deduction rules relating to an entity's superannuation activities are stated only once.

3.16 The existing law addresses each entity type specifically (eg, complying superannuation funds, non-complying superannuation funds) and states all the rules for that entity. This results in repetition as most rules apply to more than one entity. It also interferes with the logical arrangement of the provisions. The rewrite logically follows the steps in determining taxable income, that is, income included, income excluded, allowable deductions and deductions not allowed. The entities to which the rule applies are listed beside it.

3.17 The benefits of this approach are seen most clearly in the rewrite of the provisions that include certain contributions in assessable income. The existing law lists the assessable contributions for each entity. This approach obscures the fact that source of a contribution and its tax treatment in the hands of the contributor are important in determining its assessability. A person can make contributions on behalf of someone else (eg, an

employer can make one in respect of their employee) or for the person's own benefit. For the most part, they are assessable if deductible in the hands of the contributor. The rewrite groups assessable contributions according to their source.

Subdivision 295-A: Provisions of general operation

3.18 Subdivision 295-A lists the superannuation entities to which the Division applies, gives an overview of how the Division assists in working out tax payable for these entities and sets out some general rules used in applying the Division.

3.19 The Division applies to:

- superannuation funds;
- approved deposit funds;
- pooled superannuation trusts; and
- companies (other than life insurance companies) that provide a superannuation product known as an RSA.

[Schedule 1, item 1, section 295-5]

3.20 Superannuation funds and approved deposit funds that comply with the *Superannuation Industry (Supervision) Act 1993* receive concessional tax treatment. Pooled superannuation trusts and RSA providers are also taxed concessionally.

Liability to tax for a fund, an approved deposit fund or a pooled superannuation trust

3.21 The trustee of a fund, an approved deposit fund or pooled superannuation trust is liable to pay tax on the entity's taxable income. ***[Schedule 1, item 1, subsections 295-5(2) and (3)]***

3.22 A complying superannuation fund, non-complying superannuation fund or RSA provider is also liable to pay tax on no-TFN contributions income. ***[Schedule 1, item 1, subsection 295-5(2)]***

3.23 The reference to trustee also includes the manager of an entity when there is no trustee. ***[Schedule 10, item 10, new definition of 'trustee of a superannuation fund' in subsection 995-1(1)]***

3.24 Taxable income is worked out using the general income and deduction rules as modified by Division 295. Specific income and deduction rules dealing solely with superannuation activities also apply. ***[Schedule 1, item 1, section 295-10]***

3.25 The arm's length income of complying funds, complying approved deposit funds and pooled superannuation trusts is taxed at a concessional rate. The Commissioner can make an assessment in anticipation of a notice being issued by APRA, confirming that the fund or approved deposit fund complies with the *Superannuation Industry (Supervision) Act 1993* or that the trust is a pooled superannuation trust. ***[Schedule 1, item 1, section 295-25]***

Liability to tax for an RSA provider

3.26 An RSA provider is a company and, like other companies, is liable to pay tax on its taxable income (section 4-1 of the ITAA 1997).

3.27 There are some specific income and deduction rules for RSAs, including how to isolate the part of the provider's taxable income attributable to providing RSAs. ***[Schedule 1, item 1, section 295-10]***

3.28 That part is taxed at the same concessional rate as that applying to complying funds. The remainder of the provider's taxable income is taxed at the general company rate.

Exempt entities

3.29 Public sector funds or schemes established under a state Act listed in the *Income Tax Regulations 1936* are exempt. They are known as 'constitutionally protected funds'. ***[Schedule 1, item 8, section 50-25]***

3.30 Tax does not apply to the property of a state. This may be relevant to state funds or schemes not listed in the *Income Tax Regulations 1936*. ***[Schedule 1, item 1, section 295-15]***

3.31 Another Commonwealth law can only exempt a superannuation entity if it does so expressly. ***[Schedule 1, item 1, section 295-20]***

3.32 The Commissioner may make an assessment for a fund or trust that is not complying or a pooled superannuation trust on the

basis that it is likely that a notice will be given having the effect that it will become such an entity. ***[Schedule 1, item 1, section 295-25]***

Superannuation Industry (Supervision) Act 1993 notice revoked

3.33 Some of the specific income and deduction provisions depend on notices being issued by APRA under the *Superannuation Industry (Supervision) Act 1993* or its regulations. APRA is responsible for ensuring the prudent management of funds, approved deposit funds and pooled superannuation trusts.

3.34 If a notice is revoked, or the decision to give it is subsequently set aside, it is taken never to have been given ***[Schedule 1, item 1, section 295-30]***. As a result, any assessment made on the basis of the notice can be amended (consequential amendments that will be made to subsection 170(10AA) of the ITAA Act 1936).

Acronyms used in tables

3.35 Many of the specific income and deduction rules are set out in tables. The entities to which the rule applies are listed in one column and the rule in the next. The entities are referred to by acronyms to simplify the tables. Section 295-35 explains the acronyms. ***[Schedule 1, item 1, section 295-35]***

Subdivision 295-B: Modifications of provisions of the ITAA 1997

3.36 Subdivision 295-B modifies the application of some other provisions of the ITAA 1997 about income and deductions.

Capital gains tax to be a primary code for calculating gains and losses

3.37 Only the capital gains tax (CGT) provisions (and not the general income provisions) apply if a CGT event happens involving a CGT asset owned by a complying fund, a complying approved deposit fund or a pooled superannuation trust. ***[Schedule 1, item 1, subsections 295-85(1) and (2)]***

3.38 But this rule does not apply to:

- a gain or loss attributable to currency exchange rate fluctuations;
- the disposal of a security; or

- some cases where the CGT provisions disregard the gain or loss.

[Schedule 1, item 1, subsections 295-85(3) and (4)]

CGT rules for pre-30 June 1988 assets

3.39 The CGT provisions also apply to assets which a trustee (or former trustee) of a complying fund, a complying approved deposit fund or a pooled superannuation trust owned when section 295-90 commenced. The assets are deemed to have been acquired on 30 June 1988. ***[Schedule 1, item 1, section 295-90]***

General deduction provisions extended

3.40 Superannuation entities can deduct amounts incurred in obtaining contributions even if the contributions are not assessable. ***[Schedule 1, item 1, section 295-95]***

3.41 Complying funds and complying approved deposit funds can deduct amounts for investing in pooled superannuation trusts even though the income from those investments is not assessable. ***[Schedule 1, item 1, section 295-100]***

Distributions to pooled superannuation trust unit holders

3.42 Income received by a complying fund, a complying approved deposit fund or a pooled superannuation trust as a result of holding units in a pooled superannuation trust is not assessable ***[Schedule 1, item 1, section 295-105].*** They are also not subject to tax when they dispose of the units. Any CGT gain or loss is disregarded (and CGT is the primary code in this situation) ***[Schedule 1, item 1, sections 295-85 and 118-350 of the ITAA 1997].***

Subdivision 295-C: Contributions included

3.43 Subdivision 295-C explains the contributions that are assessable. It is subject to Subdivision 295-D, which gives complying funds and complying approved deposit funds the option of excluding some contributions.

3.44 There are three types of contributions:

- those made on behalf of someone else;

- those made for the contributor's own benefit; and
- those transferred from other funds.

3.45 The *Superannuation Industry (Supervision) Act 1993* and regulations outline the types of contributions particular superannuation entities are entitled to receive. This explains why particular contributions are made assessable in the hands of some entities only.

3.46 The tables in Subdivision 295-C, which set out what is included in assessable income, apply to RSA providers only to the extent that amounts are paid to RSAs they provide. ***[Schedule 1, item 1, section 295-205]***

Contributions on behalf of someone else

3.47 Generally, contributions on behalf of someone else will be made by an employer on behalf of an employee. They may be paid directly to the fund by the employer or by the Commissioner who has collected them from the employer under the *Superannuation Guarantee (Administration) Act 1992* or the *Small Superannuation Accounts Act 1995*.

3.48 They are assessable in the hands of the superannuation entity to which they are made ***[Schedule 1, item 1, section 295-160]***. However, contributions made on behalf of a spouse or temporary resident of Australia are generally not assessable ***[Schedule 1, item 1, sections 295-165, 295-175 and 295-185]***. Government co-contributions and contributions for a child are also generally not assessable ***[Schedule 1, item 1, section 295-170]***.

3.49 A complying superannuation fund can, with the agreement of the contributor, choose not to include contributions made directly to it by an employer in its assessable income. This effectively shifts liability to pay the tax on those contributions to the recipient of the benefit when it is paid out. ***[Schedule 1, item 1, section 295-180]***

Personal contributions and roll-over amounts

3.50 Only personal contributions for which the contributor has provided a valid notice of intent to deduct are assessable. These are generally contributions made by self-employed persons who

receive less than 10 per cent of their income as an employee. ***[Schedule 1, item 1, section 295-190, item 1 in the table]***

3.51 These contributions are included in assessable income in the income year in which the fund or RSA provider receives a notice from the contributor saying they will be claiming a deduction. ***[Schedule 1, item 1, subsections 295-190(2) and (3)]***

3.52 If the amount of the contributor's deduction is reduced, an adjustment is made to the taxable income calculation of the superannuation provider. If the superannuation provider is notified of the reduction after it has lodged its return, it is entitled to a deduction in the income year in which it is notified ***[Schedule 1, item 1, subsection 295-490(1), item 2 in the table]***. Alternatively, the fund or RSA provider has the option to amend its return to exclude the reduction amount, but only if that would result in a greater reduction in tax for that year than the reduction that would occur for the income year in which the notice is received ***[Schedule 1, item 1, section 295-195]***. This alternative option is currently at the Commissioner's discretion, but is now essentially a self-assessing provision for the fund or RSA provider. This change is in line with the Review of Self Assessment which recommended that all discretions which go to the determination of a taxpayer's liability be reviewed, and where practicable be replaced with tests that a taxpayer can apply at the time of lodgement.

3.53 The untaxed element of a superannuation benefit that is rolled over into a complying fund or RSA provider is also assessable in the income year in which the roll-over occurs, but only to the extent that it is not an 'excess untaxed roll-over amount'. An amount will be an excess untaxed roll-over amount if it exceeds $1 million. ***[Schedule 1, item 1, subsection 295-190(1), item 2 in the table and subsection 295-190(4)]***

Transfers from foreign funds

3.54 An Australian (resident) superannuation fund may be assessable on an amount transferred to it from a non-resident superannuation fund. ***[Schedule 1, item 1, section 295-200]***

Former constitutionally protected funds

3.55 A complying superannuation fund that was previously a constitutionally protected fund may be assessable on certain

amounts of rolled over superannuation benefits. ***[Schedule 1, item 1, section 295-210]***

Subdivision 295-D: Contributions excluded

3.56 Subdivision 295-D gives complying funds and approved deposit funds the option of reducing the contributions included in their assessable income.

Transferring liability to an investment vehicle

3.57 The superannuation provider in relation to a complying superannuation fund or a complying approved deposit fund can agree with a life insurance entity or a pooled superannuation trust to transfer contributions to it. The trustee must hold sufficient investments in the *transferee* to cover the tax payable by the transferee as a result of the transfer. ***[Schedule 1, item 1, sections 295-260 and 295-320, item 1 in the table, item 13, paragraph 320-15(1)(i)]***

Applying pre-1 July 1988 funding credits against contributions

3.58 The superannuation provider in relation to a complying superannuation fund can choose to reduce the contributions otherwise included in its assessable income by applying its available funding credits to the contributions. These credits represent the fund's unfunded liability for benefits accrued prior to funds becoming taxable on 1 July 1988. ***[Schedule 1, item 1, section 295-265]***

3.59 The superannuation provider in relation to a complying superannuation fund can also reduce the contributions otherwise included in its assessable income in anticipation of APRA confirming the amount of credits available as at 1 July 1988. However the credits will not be considered available for the income year to the extent that the notice received differs from the amount anticipated. ***[Schedule 1, item 1, section 295-270]***

Subdivision 295-E: Other income amounts

3.60 Subdivision 295-E includes some amounts in assessable income and excludes other amounts.

Amounts included

3.61 These amounts are included in assessable income:

- contributions transferred to a pooled superannuation trust by a complying fund or complying approved deposit fund ***[Schedule 1, item 1, section 295-320, item 1 in the table]***;

- an amount worked out by reference to the market value of the assets of a superannuation fund that changes its status from complying to non-complying or from non-resident to resident ***[Schedule 1, item 1, section 295-320, items 2 and 3 in the table, sections 295-325 and 295-330]***; and

- the recoupment by a complying superannuation fund or an RSA provider of an insurance premium that it has deducted ***[Schedule 1, item 1, section 295-320, items 4 and 5 in the table]***.

Amounts excluded

3.62 These amounts are excluded from assessable income:

- a bonus on a life insurance policy received by a complying superannuation fund, a complying approved deposit fund or a pooled superannuation trust (other than a reversionary bonus) ***[Schedule 1, item 1, section 295-335, item 1 in the table]***;

- income derived by a pooled superannuation trust that is attributable to an investment in it by a constitutionally protected fund ***[Schedule 1, item 1, section 295-335, item 2 in the table]***; and

- a bonus on a life insurance policy that is an RSA received by an RSA provider (other than a reversionary bonus) ***[Schedule 1, item 1, section 295-335, item 3 in the table]***.

Subdivision 295-F: Exempt income

3.63 Subdivision 295-F exempts some amounts from income tax.

Amounts used to fund current pension liabilities

3.64 The following is exempt income:

- income derived by a complying superannuation fund from assets dedicated to funding its current pension liabilities ***[Schedule 1, item 1, section 295-385]***;
- income derived by a complying superannuation fund needed to fund current pension liabilities for which assets have not been dedicated ***[Schedule 1, item 1, sections 295-390 and 295-395]***; and
- income derived by a pooled superannuation trust attributable to the current pension liabilities of unitholders that are complying superannuation funds ***[Schedule 1, item 1, section 295-400]***. A formula is used to determine the proportion that is considered exempt. The trustee can however elect to use an alternative amount for determining the proportion of exempt income in certain situations ***[Schedule 1, item 1, subsection 295-400(3)]***. This alternative option is currently at the Commissioner's discretion, but is now essentially a self-assessing provision for the trustee.

Other exempt income

3.65 The following income is also exempt:

- a grant of financial assistance under Part 23 of the *Superannuation Industry (Supervision) Act 1993* ***[Schedule 1, item 1, section 295-405, item 1 in the table]***; and
- amounts credited to an RSA from which a pension is being paid ***[Schedule 1, item 1, section 295-405, items 2 and 3 in the table and section 295-410]***.

Subdivision 295-G: Deductions

3.66 Subdivision 295-G deals with deductions relating specifically to an entity's superannuation activities. It specifies amounts that are deductible and amounts that are not.

Death or disability benefits payable

3.67 A complying superannuation fund can deduct part of the premiums it pays on insurance policies to cover its liability to pay death or disability benefits to fund members. It can also deduct the

amount it could reasonably expect to pay for such a policy if it does not have one. ***[Schedule 1, item 1, sections 295-460, 295-465 and 295-480]***

3.68 Alternatively, the fund can choose to deduct an amount for its future liability to pay death or disability benefits. ***[Schedule 1, item 1, section 295-470]***

3.69 An RSA provider can also deduct premiums it pays on insurance policies to cover its liability to pay death or disability benefits. ***[Schedule 1, item 1, section 295-475]***

Increased amount of superannuation lump sum death benefits

3.70 A complying superannuation fund or a complying approved deposit fund can deduct an amount to ensure that the amount of death benefits paid to a spouse, former spouse or child is not reduced as a result of contributions being taxed. It is not appropriate to allow the deduction if those individuals cannot reasonably be expected to benefit from the estate. Therefore, the deduction is only available to the extent that the spouse, former spouse or child of the deceased can reasonably be expected to benefit from the estate. ***[Schedule 1, item 1, section 295-485]***

3.71 Where a death benefit is paid to a deceased estate the deduction is reduced to the extent that the intended recipient cannot reasonably be expected to benefit ***[Schedule 1, item 1, subsection 295-485(4)]***. The deduction available is currently at the discretion of the Commissioner, who has regard to the extent to which the recipient can be expected to benefit from the payment. This is replaced with an objective test of reasonableness.

Other deductions

3.72 These amounts can also be deducted:

- contributions included in assessable income that are fringe benefits (because they will be taxed as fringe benefits in the hands of the contributor);
- personal contributions to the extent the contributor's deduction for them has been reduced (but only if the superannuation fund or RSA provider has not exercised the option in section 295-195);

- a levy imposed under the *Superannuation (Financial Assistance Funding) Levy Act 1993*; and
- contributions paid back to an employer by a superannuation fund that has never complied with the *Superannuation Industry (Supervision) Act 1993* (to ensure overall consistency with payments of benefits by such funds to their members).

[Schedule 1, item 1, section 295-490]

Amounts that cannot be deducted

3.73 These amounts cannot be deducted:

- benefits paid by superannuation funds or RSA providers ***[Schedule 1, item 1, section 295-495, items 1 to 3 in the table]***;
- amounts credited to RSAs ***[Schedule 1, item 1, section 295-495, item 4 in the table]***; and
- a repayment of financial assistance under the *Superannuation Industry (Supervision) Act 1993* ***[Schedule 1, item 1, section 295-495, item 5 in the table]***.

Subdivision 295-H: Components of taxable income

3.74 Subdivision 295-H works out the components of the taxable income of complying funds, complying approved deposit funds, pooled superannuation trusts and RSA providers for the purpose of applying tax rates.

Complying superannuation funds, complying approved deposit funds and pooled superannuation trusts

3.75 The income of a complying superannuation fund, complying approved deposit fund or pooled superannuation trust is split into a 'non-arm's length component' and a 'low tax component'. ***[Schedule 1, item 1, section 295-545]***

3.76 The non-arm's length component comprises non-arm's length dividends received from private companies, non-fixed interest trust distributions, and any income derived from

transactions where the parties are not dealing with each other at arm's length ***[Schedule 1, item 1, subsection 295-545(2) and section 295-550].*** This component is reduced by any deductions attributable to that income and is then taxed at the highest marginal rate. 'Derived' in this context is applicable to both ordinary and statutory income.

3.77 The remaining part of the entity's taxable income is the low tax component which is taxed at a concessional rate (currently 15 per cent). ***[Schedule 1, item 1, subsection 295-545(3)]***

3.78 In Part IX of the ITAA 1936, the Commissioner has a discretion to decide that it is unreasonable that a dividend from a private company be treated as 'special income' (or 'non-arm's length income') where it is derived by a complying superannuation fund, complying approved deposit fund, or a pooled superannuation trust. This is replaced with an objective test that the amount be consistent with an 'arm's length dealing'. ***[Schedule 1, item 1, subsections 295-545(2) and (3)]***

RSA providers

3.79 RSA providers must work out the assessable income attributable to providing RSAs (the 'RSA component') so it can be taxed at the same concessional rate as applies to complying funds. The balance of their income (the 'standard component') is taxed at the standard company rate. ***[Schedule 1, item 1, section 295-555]***

3.80 RSA providers are effectively taxed as if their RSA activities and their other activities are carried on by two separate entities. This ensures they are treated consistently with funds and pooled superannuation trusts which only have superannuation activities.

3.81 RSA income cannot be offset against a loss from the provider's other activities. So if the RSA component is more than the provider's total taxable income it will have both a taxable income and a loss. Its taxable income will equal the RSA component but it will also be entitled to carry forward a loss in relation to its other activities. ***[Schedule 1, item 1, subsection 295-555(3)]***

New Dictionary terms

3.82 Section 995-1 of the ITAA 1997 will be amended to insert additional definitions in the Dictionary. The definitions, and their

equivalents in the old law, are identified and commented on in Table 3.1.

Table 3.1

New term	*Current term*	*Commentary*
low tax component	Standard component.	Describes the component of taxable income taxed concessionally.
non-arm's length component	Special component.	Describes the component of taxable income taxed at the top marginal rate.
non-arm's length income	Special income.	Describes the income included in the high tax component.
Australian superannuation fund	Resident superannuation fund.	Describes what funds will be considered Australian residents for tax purposes.
foreign superannuation fund	Non-resident superannuation fund.	Describes what funds will be considered foreign residents for tax purposes.

3.83 The Dictionary in the ITAA 1997, will also be amended to include terms previously defined in Part IX of the ITAA 1936.

Provisions of Part IX of the ITAA 1936 that have been changed for clarity

3.84 The minor changes in various provisions that are made for clarity do not change how the law operates under Part IX of the ITAA 1936 in regard to those provisions. The changes simply clarify how the provisions currently operate.

Section 295-90: Deductions for contributions

3.85 Superannuation entities can deduct amounts incurred in obtaining contributions even if the contributions are not assessable.

3.86 The rewritten section (section 295-90) clarifies that the provision applies to *all* contributions that are not assessable.

3.87 The way the section is worded in Part IX of the ITAA 1936 is unclear in regard to this, as it refers to contributions mentioned in specific sections. There is doubt about whether those sections

refer to contributions such as non-deductible personal contributions.

Section 295-195: Exclusions of personal contributions

3.88 Superannuation funds and RSA providers do not include contributions in their assessable income unless the contributor advises they will be claiming a deduction.

3.89 The rewritten section states expressly that a notice from the contributor reducing the amount of a deduction has the effect of reducing the assessable income of the fund or provider if the reduction notice is received *before* the fund or provider lodges its return for the income year to which the contribution relates.

3.90 This is implicit in the current law but only the effects of a reduction notice received *after* lodgement are dealt with specifically.

Provisions amended for minor policy changes

3.91 The definition of 'Australian superannuation fund' replaces the existing definition of 'resident superannuation fund' in section 6E of the ITAA 1936 with the scope of the definition dealt with in a much simpler way. The main change is that there is no longer a specific temporary absence rule for trustees of the fund as an alternative condition to the requirement that the central management and control of the fund be in Australia.

3.92 The alternative test to the central management and control test (the two-year temporary absence rule) is generally satisfied if:

- the trustees of the fund (or a director or directors of the corporate trustee) were temporarily absent from Australia;
- the central management and control of the fund would have been in Australia if the trustees (or directors) were in Australia; and
- the continuous period for which the trustee (or directors) had been outside Australia at that time did not exceed two years.

3.93 The definition of Australian superannuation fund does not use this alternative test. It deals with temporary absences of trustees by requiring that the central management and control of the fund *ordinarily* be in Australia. Satisfying the current two-year temporary absence rule described above (set out in subsections 6E(1A) and (1B) of the ITAA 1936) would normally satisfy the *ordinarily* requirement. That is, the trustee's time outside Australia does not exceed two years.

Example 3.1

> A married couple are trustees of their self-managed superannuation fund that was established in 2001. In July 2007 the husband accepts a two year employment contract to work for an overseas government, intending to return to Australia after the contract is fulfilled. His wife joins him for the term of his contract. They make no contributions to the fund after leaving Australia.
>
> In these circumstances it is accepted that the central management and control of the self-managed superannuation fund is ordinarily in Australia and the self-managed superannuation fund will be treated as an Australian superannuation fund. If the husband's employment contract was continually extended so that the couple remained overseas for a period considerably in excess of two years, central management and control of the self-managed superannuation fund would not ordinarily be in Australia and the self-managed superannuation fund would not be treated as an Australian superannuation fund.

Provisions of Part IX of the ITAA 1936 that have been inserted or amended due to the *Simplified Superannuation* reforms

Subdivision 295-I: No TFN contributions income

3.94 Subdivision 295-I provides a new category of income for superannuation and RSA providers that receive superannuation contributions which are included in assessable income where no TFN is attached to the receiving member's account.

3.95 Subdivision 295-I does not apply to RSA providers which are life insurance companies as they are taxed under Division 320 of the ITAA 1997. ***[Schedule 1, item 1, section 295-5]***

3.96 Superannuation and RSA providers are liable to pay tax on no-TFN contributions income. The tax applies to contributions made to a complying superannuation fund, non-complying superannuation fund or an RSA. ***[Schedule 1, item 1, section 295-605]***

3.97 Tax is imposed by the *Income Tax Rates Act 1986*.

3.98 A particular rate of tax is imposed on no-TFN contributions income. ***[Schedule 1, item 18, section 29 of the Income Tax Rates Act 1986]***

3.99 Section 169 of the ITAA 1936 allows the Commissioner to make an assessment of the amount of no-TFN contributions income tax.

3.100 ***No-TFN contributions income*** applies to contributions included in the superannuation provider's assessable income by Subdivision 295-C for the income year in which 1 July 2007 occurs (or later income years) only if the contributions are made on or after 1 July 2007 and no TFN has been quoted by the end of the income year in which the contribution is made. ***[Schedule 1, item 1, subsection 295-610(1)]***

3.101 Where no TFN has been quoted by the last day of the income year and a contribution is withdrawn or transferred out of the superannuation fund or RSA provider prior to the end of the income year, the individual will be taken not to have quoted his or her TFN.

3.102 Contributions will not form part of the no-TFN contributions income if the superannuation interest or RSA existed prior to 1 July 2007 and the total contributions included in the superannuation fund or RSA provider's assessable income for an income year is $1,000 or less. ***[Schedule 1, item 1, subsection 295-610(2)]***

3.103 An individual will be taken to have quoted their TFN to the superannuation provider if they have quoted or are taken to have quoted their TFN for superannuation purposes under the ITAA 1997, the *Superannuation Industry (Supervision) Act 1993* or the *Retirement Savings Account Act 1997*. ***[Schedule 1, item 1, section 295-615]***

3.104 A superannuation fund or RSA provider cannot reduce their no-TFN contributions income using any of the provisions in Subdivision 295-D. ***[Schedule 1, item 1, section 295-620]***

3.105 Where the Commissioner makes an assessment of no-TFN contributions income tax, the notice of assessment may be included in a notice of any other assessment under the ITAA 1997. ***[Schedule 1, item 1, subsection 295-625(1)]***

3.106 Where certain conditions are met the Commissioner is taken to have made a no-TFN contributions income tax assessment. ***[Schedule 1, item 1, subsection 295-625(2)]***

3.107 The assessment conditions are met where a superannuation provider first provides the Commissioner with an income tax return for an income year and the Commissioner has not already made a no-TFN contributions income tax assessment for the provider for that year. ***[Schedule 1, item 1, subsection 295-625(3)]***

3.108 The no-TFN contributions income tax assessment is taken to have been made on the day of the return and is taken to be an assessment of the amount of income tax payable on the no-TFN contributions income of the provider. ***[Schedule 1, item 1, subsection 295-625(4)]***

3.109 A return is considered to be a notice of assessment signed by the Commissioner and given to the provider on the day of the return. ***[Schedule 1, item 1, subsection 295-625(5)]***

Division 295-J: No-TFN income tax offset

3.110 Subdivision 295-J allows a superannuation provider to obtain a refund of no-TFN contributions income tax paid where a TFN is subsequently quoted.

3.111 A superannuation provider may obtain a tax offset for amounts of tax paid on no-TFN contributions income for an income year commencing on or after 1 July 2007. ***[Schedule 1, item 1, subsection 295-675(1)]***

3.112 The tax offset can only be claimed for tax paid on no-TFN contributions income of an earlier year. A provider cannot pay no-TFN contributions income tax for a contribution and claim a tax offset for that same contribution in the same income year. ***[Schedule 1, item 1, subsection 295-675(1)]***

3.113 The tax offset is only available if an individual quotes their TFN in the current year, and no-TFN contributions income tax of

that individual's contribution was payable in one of the three most recent income years. ***[Schedule 1, item 1, subsection 295-675(2)]***

3.114 For example, if a contribution was no-TFN contributions income for the 2007-08 income year the tax offset can only be claimed in the year the individual first quotes their TFN up until the end of the 2010-11 income year.

3.115 While the superannuation provider is entitled to claim the tax offset, the amount of the offset is to be credited to the individual's account.

3.116 The tax offset is a refundable tax offset and the rules contained in Division 67 of the ITAA 1997 apply.

3.117 The amount of the tax offset for an income year is the sum of the amount of tax payable on no-TFN contributions income for which a TFN has subsequently been quoted. ***[Schedule 1, item 1, section 295-680]***

3.118 Contributions which do not satisfy the conditions specified in section 295-675 do not count towards the sum of the tax offset.

Part IIG: Interest on certain offsets relating to no-TFN contributions income of superannuation funds and RSA providers

3.119 In certain circumstances interest will be payable to a superannuation provider under the *Taxation (Interest on Overpayments and Early Payments) Act 1993* where an individual quotes a TFN to the provider resulting in a tax offset under Subdivision 295-J of the ITAA 1997.

3.120 Where:

- an individual has quoted their TFN to their employer before the end of an income year;
- their employer failed to comply with the requirements set out in section 299C of *Superannuation Industry (Supervision) Act 1993* which requires them to inform the superannuation provider to which they make contributions of the individual's TFN before the end of the income year;

- due to the employers failure to comply with section 299C of the *Superannuation Industry (Supervision) Act 1993* contributions made to that superannuation provider formed part of its no-TFN contributions income;

- tax payable on that no-TFN contributions income counted towards the no-TFN contributions tax offset of the superannuation provider for the current year; and

- the tax offset has been applied in an assessment in respect of the superannuation provider for the current year,

then interest will be payable. ***[Schedule 1, item 36, section 8ZD of the Taxation (Interest on Overpayments and Early Payments) Act 1993]***

3.121 The interest is payable for a period from the day the no-TFN contributions income tax was paid or the day the tax was required to be paid (whichever is the later) until the day on which the assessment of the no-TFN income tax offset is made. ***[Schedule 1, item 36, section 8ZE of the Taxation (Interest on Overpayments and Early Payments) Act 1993]***

3.122 The interest rate is the base interest rate in section 8AAD of the *Taxation Administration Act 1953*. ***[Schedule 1, item 36, section 8ZF of the Taxation (Interest on Overpayments and Early Payments) Act 1993]***

3.123 Interest payable under the *Taxation (Interest on Overpayments and Early Payments) Act 1993* is assessable income under section 15-35 of the ITAA 1997.

Treatment of late contributions

3.124 Some superannuation funds finance benefits by making large one-off contributions. As mentioned above, the ‘trustee’ of a complying superannuation fund can, with the consent of the contributor, elect for these contributions not to be included in assessable income. This effectively shifts liability to tax on those contributions to the recipient of the benefit when it is finally paid out. ***[Schedule 1, item 1, section 295-180]***

3.125 Some funds also allow their members to elect whether their benefits are paid from a taxed or untaxed source. Trustees will not be able to make this election (and therefore will not be able

to offer this choice) where the superannuation plan comes into operation after 5 September 2006. ***[Schedule 1, item 1, subsection 295-180(5)]***

Transitional arrangements for employment termination payments existing at 9 May 2006

3.126 As part of the *Simplified Superannuation* reforms the taxation of employment termination payments are changed to reflect the removal of the reasonable benefit limits system and benefits tax. Employment termination payments will have two components (tax free and taxable). The taxable component is taxed at no more than 15 per cent for amounts up to $140,000, the excess up to $1 million is taxed at the top marginal rate (plus the Medicare levy).

3.127 Since superannuation benefits paid to those over age 60 are tax free, employment termination payments will not be able to be rolled over into superannuation. Allowing roll-overs would have enabled people to put in place arrangements to avoid the intent of other parts of the reforms, namely the caps on contributions.

3.128 There are transitional arrangements in place for individuals with an entitlement to a payment on termination of employment specified in existing employment contracts as at 9 May 2006, provided payment is made prior to 1 July 2012. These payments are able to be directed into superannuation until 1 July 2012. Amounts of the taxable component of a directed termination payment paid into a superannuation fund are included in the assessable income of the fund ***[Schedule 1, item 1, section 295-190, item 3 in the table]***. If the value of the taxable component of the directed termination payment exceeds $1 million then the excess is subject to additional taxation at the top marginal tax rate plus the Medicare levy.

Deductions for future liability to pay benefits

3.129 As mentioned above, complying superannuation funds can deduct part of their insurance premiums covering liability to pay death or disability benefits to fund members or choose to deduct an amount for their future liability to pay death or disability benefits. ***[Schedule 1, item 1, sections 295-460, 295-465, 295-470 and 295-480]***

3.130 A complying superannuation fund's choice to deduct an amount for the future liability to pay a death or disability benefit is limited to employees. The concessional tax treatment of employee invalidity benefits is extended to the self-employed. Consistent with this extension to the self-employed, the choice to deduct an amount for the future liability to pay a death or disability benefit is similarly extended to the self-employed.

Provisions of Part IX of the ITAA 1936 that have not been rewritten

3.131 Some provisions of the ITAA 1936 have not been rewritten into the ITAA 1997 for various reasons. The various provisions, what they are about, and the reason for their omission are commented on in Table 3.2.

Table 3.2

Provision	*Subject*	*Reason for omission*
267(1)	Definition of actuary's certificate.	Included in the operative rule.
267(1)	Definition of arm's length premium.	Included in the operative rule.
267(1)	Definition of certificate date.	Included in the operative rule.
267(1)	Definition of continuously complying approved deposit fund.	Included in the operative rule.
267(1)	Definition of continuously complying superannuation fund.	Included in the operative rule.
267(1)	Definition of continuously non-complying superannuation fund.	Included in the operative rule.
267(1)	Definition of current pension liability.	Included in the operative rule.
267(1)	Definition of death or disability benefit.	Included in the operative rule.
267(1)	Definition of dependant.	Included in the operative rule.
267(1)	Definition of eligible approved deposit fund.	The form of the rewritten provisions makes it unnecessary.

Provision	***Subject***	***Reason for omission***
267(1)	Definition of eligible entity.	The form of the rewritten provisions makes it unnecessary.
267(1)	Definition of eligible superannuation fund.	The form of the rewritten provisions makes it unnecessary.
267(1)	Definition of non-current pension liability.	Included in the operative rule.
267(1)	Definition of non-reversionary bonus.	Included in the operative rule.
267(1)	Definition of normal assessable income.	Included in the operative rule.
267(1)	Definition of specified roll-over amount.	Included in the operative rule.
267(1)	Definition of superannuation liability.	Included in the operative rule.
267(1)	Definition of superannuation policy.	Redundant. References to this term were removed in 1989.
267(1)	Definition of taxable contribution.	Included in the operative rule.
267(1)	Definition of unit trust.	The form of the rewritten provisions makes it unnecessary.
267(4)	A reference to section 342 of the *Superannuation Industry (Supervision) Act 1993* includes section 15D of the repealed *Occupational Superannuation Standards Act 1987*.	Redundant. References to section 342 of the *Superannuation Industry (Supervision) Act 1993* in the rewritten law are prospective.
268	Trustees of funds not constituted as trusts are taken to be trustees of the fund for the purposes of Part IX.	The definition of 'trustee' in section 995-1 now incorporates this idea.
269B	Nothing in the general exemption provisions exempts the trustee of a fund or a pooled superannuation trust from a liability to pay tax in relation to its superannuation activities.	Not required. Section 960-100 of the ITAA 1997 clarifies that the trustee in this capacity is a separate entity. Liability is imposed by section 4-1 of the ITAA 1997.

Provision	***Subject***	***Reason for omission***
274(10)(a), 274(10)(b)	Contributions received by a non-complying superannuation fund from another fund are assessable.	Redundant. They were relevant when complying funds could not retain excess benefits, but that is no longer the case.
275(2)(a)	Contributions transferred to a life insurance company are included in their assessable income.	To be included in the consequential amendments to Division 320 of the ITAA 1997 (Life insurance companies).
276(5)	The section about the consequences for the fund of a contributor's deduction being reduced applies once only for a particular contribution.	Unnecessary. The contributor's deduction entitlement and their notice obligations are fully set out in other provisions.
279D(1)(a)(ii)	Life insurance companies are allowed a deduction to ensure that benefits paid on certain annuity policies are not reduced as a result of taxing contributions transferred to them.	To be included in consequential amendments to Division 320 of the ITAA 1997 (Life insurance companies).
282	Amounts accrued to a complying superannuation fund prior to 1 July 1988 are not assessable.	The rewritten provisions apply prospectively.
290A	Exempts income of approved deposit funds attributable to 25 May 1988 deposits.	To go into the *Income Tax (Transitional Provisions) Act 1997* with ongoing application.
291	Amounts accrued to a complying approved deposit fund prior to 1 July 1988 are not assessable.	The rewritten provisions apply prospectively.
297	Amounts accrued to a pooled superannuation trust prior to 1 July 1988 are not assessable.	The rewritten provisions apply prospectively.
300(1)(a), 300(2)(a)	Superannuation funds, approved deposit funds and pooled superannuation trusts are entitled to the rebate provided by section 160AB of the ITAA 1936.	Redundant. The rebate is for interest on monies borrowed before 1 November 1968 and is no longer applicable.

Provision	Subject	Reason for omission
300(1)(b), 300(2)(b)	Superannuation funds, approved deposit funds and pooled superannuation trusts are not entitled to the dividend rebate under section 46 or 46A of the ITAA 1936.	Redundant.
308, 309, 310, 311	CGT rules for assets held by superannuation entities when they became taxable in 1988.	To go into the *Income Tax (Transitional Provisions) Act 1997* with ongoing application.

Provisions of Part VA of the ITAA 1936 that have been inserted due to the *Simplified Superannuation* reforms

Section 202DHA: A TFN quoted for Division 3 purposes is taken to have been quoted for superannuation purposes

3.132 When an individual makes a TFN declaration to their payer (their employer) they are also authorising their employer to provide their TFN to the superannuation provider to which their employer is making contributions.

3.133 Under subsection 202C(1) of the ITAA 1936 an individual who is a recipient of eligible pay as you go (PAYG) payments may make a TFN declaration under Division 3, Part VA of the ITAA 1936, thus quoting their TFN to their payer (their employer).

3.134 If that individual is also a beneficiary of an 'eligible superannuation entity' or of a 'regulated exempt public sector superannuation scheme', by completing a TFN declaration, they are also authorising their payer (their employer) to quote their TFN to the trustee of their superannuation fund to which their employer is making contributions. ***[Schedule 1, item 27, section 202DHA]***

3.135 For example, if an individual completes a TFN declaration in relation to their employment and they are a member of a superannuation fund, and their employer is making superannuation contributions for their benefit, the individual is also authorising their employer to quote their TFN to the trustee of the superannuation fund to which their employer makes contributions.

Provisions of the *Superannuation Industry (Supervision) Act 1993* that have been amended due to the *Simplified Superannuation* reforms

Subsection 6(1): Administration of Divisions 1 and 3A of Part 25A

3.136 Section 6 has been amended to allow the Commissioner to regulate a payer's (employer's) legal responsibilities to quote TFNs to superannuation entities.

3.137 APRA has the general administration of the listed provisions to the extent that administration of the provisions is not conferred on the Commissioner by paragraphs (e) or (g). ***[Schedule 1, item 28, paragraph 6(1)(a)]***

3.138 APRA has the general administration of Part 25A except Division 1 which relates to the quotation of employees' TFNs. ***[Schedule 1, item 29, subparagraph 6(1)(a)(xii)]***

3.139 The Commissioner has the general administration of the Part 24 and Divisions 2 to 5 of Part 25A to the extent that they relate to self-managed superannuation funds. ***[Schedule 1, item 30, subparagraph 6(1)(e)(v)]***

3.140 The Commissioner has general administration of Division 1 of Part 25A relating to the quotation of an individual's TFN by their payer (their employer) and Division 3A of Part 25A relating to the incorrect quotation of TFNs. ***[Schedule 1, item 31, paragraph 6(1)(g)]***

3.141 An employee can quote their TFN to their payer (their employer) in connection with the operation or the possible future operation of the *Superannuation Industry (Supervision) Act 1993* and the other 'Superannuation Acts' or after 1 July 2007 in connection with the operation of Division 3 of Part VA of the ITAA 1936. If the other conditions in section 299C are satisfied the employer must then inform the trustee of the entity to which they make contributions, of the employee's TFN. ***[Schedule 1, item 32, paragraph 299C(1)(a)]***

3.142 For example, where an employee quotes their TFN in connection with PAYG payments it is also taken to have been quoted in connection with the *Superannuation Industry (Supervision) Act 1993*. Accordingly, where this quotation has occurred an employer has a responsibility, subject to the other conditions in section 299C, to quote the employee's TFN to the superannuation

entity to which they make employer contributions, for the employee.

Paragraph 299P(a): Methods of quoting a TFN

3.143 An individual is taken to have quoted their TFN to another person if the individual informs the other person of the number in a manner approved by the regulator or in the specified approved form, or the individual is taken to have quoted their TFN in relation to the *Superannuation Industry (Supervision) Act 1993* and the 'Superannuation Acts' under any of the provisions in Division 3 of the *Superannuation Industry (Supervision) Act 1993*. ***[Schedule 1, item 34, paragraph 299P(a)]***

Division 3A: Incorrect quotation of a TFN

3.144 Where an assumed TFN recorded by a trustee is assessed by the Commissioner to either be cancelled, withdrawn or wrong, and the Commissioner can identify the beneficiary's TFN, the Commissioner may give notice of the TFN to the trustee. ***[Schedule 1, item 35, subsection 299TA(1)]***

3.145 Where the Commissioner provides the beneficiary's TFN to the trustee, the beneficiary is taken to have quoted their TFN at the time and in the way the assumed TFN was quoted to the trustee. ***[Schedule 1, item 35, subsection 299TA(2)]***

3.146 Where an assumed TFN recorded by a trustee is assessed by the Commissioner to either be cancelled, withdrawn or wrong, and the Commissioner is not satisfied that the beneficiary has a TFN, the Commissioner may provide a notice to the trustee. ***[Schedule 1, item 35, subsection 299TB(1)]***

3.147 The notice provided to the trustee must identify the beneficiary and state that the Commissioner is not satisfied that the beneficiary has a TFN. ***[Schedule 1, item 35, subsection 299TB(2)]***

3.148 The Commissioner must provide a copy of this notice to the beneficiary. ***[Schedule 1, item 35, subsection 299TB(3)]***

3.149 If a notice under section 299TB is given to a trustee, the beneficiary is taken to have not quoted their TFN to the trustee at any time.

Application and transitional provisions

Application

3.150 These amendments apply from the 2007-08 and later income years. ***[Schedule 1, item 2]***

3.151 These amendments to Part 4 apply to TFN declarations made on or after 1 July 2007. ***[Schedule 1, item 37]***

Transitional provisions

No-TFN contributions and no-TFN tax offset

3.152 Transitional provisions have been introduced for Subdivisions 295-I and 295-J which apply to a superannuation fund or RSA provider whose 2006-07 income year ends after 1 July 2007. ***[Schedule 1, item 25, section 295-610]***

3.153 For these entities, the period of their 2006-07 income year after 1 July 2007 will be taken to be part of their 2007-08 income year for the purposes of Subdivisions 295-I and 295-J.

3.154 No-TFN contributions income for the 2006-07 income year (received on or after 1 July 2007) will be included in their 2007-08 income year and treated as if they had actually been made in the superannuation fund or RSA provider's 2007-08 income year.

Example 3.2

The XYZ superannuation fund's 2006-07 income year ends on 30 September 2007. It accumulates $100,000 of no-TFN contributions income between 1 July 2007 and the end of its 2006-07 income year on 30 September 2007.

As the XYZ superannuation fund's 2006-07 income year ends after 1 July 2007, the period between 1 July 2007 and 30 September 2007 is taken to be part of its 2007-08 income year.

The $100,000 of no-TFN contributions made prior to 30 September 2007 (in its 2006-07 income year) will be taken to have been contributed in its 2007-08 income year.

Consequential amendments

Income Tax Assessment Act 1936

3.155 An assessment under section 295-610 is intended to fall within the definition of 'assessment'. ***[Schedule 1, item 3, subsection 6(1)]***

3.156 A full self assessment taxpayer must, in a return for an income year specify its taxable income or its net income, the amount of tax payable and the amount of interest payable by the taxpayer under section 102AAM. If the full assessment taxpayer is a company and is a superannuation fund or RSA provider the company must also specify its no-TFN contributions income and the amount of the income tax payable on that income. ***[Schedule 1, item 4, section 161AA]***

Income Tax Assessment Act 1997

3.157 A consequential amendment is needed to include constitutionally protected funds as exempt (Government) entities so as to ensure all their income is exempt from income tax in the appropriate way under the ITAA 1997, since it was exempt in Part IX of the ITAA 1936. ***[Schedule 1, item 7, section 11-15 and item 8, section 50-25]***

3.158 A number of consequential amendments are needed to replace references to Part IX of the ITAA 1936 with the equivalent Division 295 provisions. ***[Schedule 1, Part 2, item 5, section 9-1, item 6, section 9-5, item 40, subparagraph 320-15(1)(i), item 14, subsection 320-15(3)]***

3.159 A number of consequential amendments are needed to incorporate new definitional terms arising in the rewrite. ***[Schedule 1, item 10, Subdivision 118-G, item 11, paragraph 118-515(1)(b), item 12, section 118-520, item 50, section 995-1, definition of 'Australian superannuation fund', item 55, section 995-1, definition of 'endowment policy', item 60, section 995-1, definition of 'foreign superannuation fund', item 65, section 995-1, definition of 'non-arm's length income', item 70, section 995-1, definition of 'quoted (for superannuation purposes)', item 75, section 995-1, definition of 'RSA component', item 80, section 995-1, definition of 'segregated current pension assets', item 85, section 995-1, definition of 'segregated non-current assets', item 90, section 995-1, definition of 'standard component', item 95, section 995-1, definition of 'superannuation fund for foreign residents', item 100, section 995-1, definition of 'whole of life policy']***

3.160 A number of amendments are needed in Division 320 (relating to life insurance companies), as some provisions applying

to these entities were in Part IX. However, when rewritten into the ITAA 1997, they are more appropriately located in Division 320 which contains rules applying to life insurance companies. ***[Schedule 1, item 13, paragraph 320-15(1)(i), item 14, subsection 320-15(3), item 15, section 320-107]***

3.161 The refundable rules for tax offsets apply to the tax offset in respect of no-TFN contributions income under Subdivision 295-J. ***[Schedule 1, item 9, section 67-25]***

3.162 The definition of 'quoted for superannuation purposes' has the same meaning as in section 295-615.

Income Tax Rates Act 1986

3.163 A separate rate of tax applies to no-TFN contributions income (defined by section 295-675). ***[Schedule 1, item 18, subsection 29(1)]***

3.164 The separate rate of tax is applicable to a trustee of a complying superannuation fund, a non-complying superannuation fund or company (other than a life insurance company) that is an RSA provider.

3.165 The rate of tax is calculated as the top marginal tax rate (Column 2 of the table in Part I of Schedule 7 to the *Income Tax Rates Act 1986*) plus the Medicare levy. The rate of tax generally payable on contributions (under paragraph 26(1)(a), subsection 26(2) or paragraph 23(4BA)(a)) is then subtracted from this rate. ***[Schedule 1, item 18, subsection 29(2)]***

3.166 For example, for the 2007-08 income year, Column 2 of the table in Part I of Schedule 7 to this Act specifies a rate of tax at 45 per cent. The Medicare levy tax rate of 1.5 per cent is then added to this amount, totalling 46.5 per cent. The rate of tax under paragraph 26(1)(b) for a complying superannuation fund (15 per cent) is then subtracted from 46.5 per cent.

3.167 The rate of tax applicable to no-TFN contributions income is 31.5 per cent.

3.168 The amount of tax payable for no-TFN contributions income is payable in addition to the ordinary income tax payable on contributions.

3.169 For example, for 2007-08 no-TFN contributions income will be taxed at a rate of 31.5 per cent. This income will also form part of the superannuation fund or RSA provider's assessable income and be taxed as part of its taxable income (generally at a rate of 15 per cent). ***[Schedule 1, item 1, paragraph 26(1)(a), subsection 26(2) or paragraph 23(4BA)(a) of the Income Tax Rates Act 1986]***

Finding Table 1 — New law to old law

New law	*Current law*
295-1	No equivalent
295-5(1)	270
295-5(2)	278, 286, 289, 294
295-5(3)	296(1)
295-5(4)	299A
295-10	272
295-15	271
295-20	269A
295-25	300A
295-30	269(2), 301
295-35	No equivalent
295-85	304
295-90	306
295-90(4)	315
295-95(1)	277, 277AA
295-95(2)	6E(1), (1A), (1B), (1C), (3)
295-95(3)	6E(4A), (4B)
295-100	279E, 289A
295-105	296(2)
295-155	No equivalent
295-160 item 1	274(1)(a)(i), (ba)(i)
295-160 item 2	274(1)(aa)
295-160 item 3	274(1)(b)(ii), (ba)(iv), (d)
295-160 item 4	274(1)(e)

New law	*Current law*
295-165	274(1)(a)(i)(C), (ba)(i)(A)
295-170	274(1)(a)(i)(D), (E), (ba)(i)(B), (C), (1)(e)
295-175	274(4), (5)
295-180(1), (2)	274(7)
295-180(3)	274(8)
295-180(4)	274(9)
295-180(5)	No equivalent
295-185	274(1)(aa)
295-190(1) item 1	274(1)(b)(i), (ba)(iii)
295-190(1) item 2	274(1)(a)(ii), (ba)(ii), (c)
295-190(1), item 3	No equivalent
295-190(2), (3)	274(1)(b)(i), (ba)(iii), 274(2), (3)
295-190(4)	274(1)(a)(ii), (ba)(ii), (c)
295-195(1)	No equivalent
295-195(2), (3)	276(3)
295-200	274(10)(c), (10)(d)
295-205	No equivalent
295-210	281A
295-260	275
295-265(1), (5), (6), (7), (8)	275B
295-265(2), (3), (4)	275A
295-270	300B
295-320 item 1	275(2)(a)
295-320 item 2	288A
295-320 item 3	288B
295-320, item 4	279A
295-320, item 5	299F
295-325	288A
295-330	288B
295-335 item 1	282A, 291A, 297A
295-335 item 2	297C

New law	*Current law*
295-335, item 3	No equivalent
295-385	273A, 282B
295-390	283
295-395	273B
295-400	297B
295-405 item 1	315C
295-405 items 2 and 3	299G
295-410	299C(6)
295-460	267(1) *death or disability benefit*
295-465	279
295-470	279B
295-475	299E(1)
295-480(1)	267(1) *whole of life policy*
295-480(2)	267(1) *endowment policy*
295-485	279D
295-490(1) item 1	277A
295-490(1) item 2	276(1), (2)
295-490(1) item 3	315A, 315B
295-490(1) item 4	286A
295-490(2)	315E
295-490(3)	315F
295-495 item 1	280
295-495 item 2	287
295-495 item 3	299E(2)
295-495 item 4	299E(3)
295-495 item 5	315D
295-545(1)	284, 285, 292, 293, 298, 299
295-545(2)	267(1) *special component*, 284, 292, 298
295-545(3)	267(1) *standard component*, 285, 293, 299
295-550	273
295-555(1)	299D(1)

New law	*Current law*
295-555(2)	267(1) RSA component, 299C, 299D(2)
295-555(3)	299CA
295-555(4)	267(1) standard component , 299D(3)
295-605	No equivalent
295-610	No equivalent
295-615	No equivalent
295-620	No equivalent
295-625	No equivalent
295-675	No equivalent
295-680	No equivalent

Finding Table 2 —— Old law to new law

Current law	*New law*
267(1) Interpretation	
actuary	995-1(1)
actuary's certificate	Omitted
annuity	Omitted
arm's length premium	Omitted
certificate date	Omitted
complying ADF	995-1(1) *complying approved deposit fund*
complying superannuation fund	995-1(1)
constitutionally protected fund	995-1(1)
continuously complying ADF	Omitted
continuously complying superannuation fund	Omitted
continuously non-complying superannuation fund	Omitted
current pension liability	Omitted

Current law	*New law*
death or disability benefit	Omitted
dependant	Omitted
eligible ADF	Omitted
eligible entity	Omitted
eligible superannuation fund	Omitted
eligible termination payment	Omitted
endowment policy	295-480(2)
last retirement date	995-1(1), *last retirement day*
non-complying ADF	995-1(1) *non-complying approved deposit fund*
non-complying superannuation fund	995-1(1)
non-current pension liability	Omitted
non-reversionary bonus	Omitted
normal assessable income	Omitted
pension	Omitted
pooled superannuation trust	995-1(1)
post-June 83 component	995-1(1), 307-275 *element taxed in the fund*
pre-July 83 component	Omitted
registered organisation	Omitted
RSA component	295-555(2)
segregated current pension assets	295-385(3)
segregated non-current pension assets	295-395
SIS Act	995-1(1)
special component	295-545(2) *non-arm's length component*
special income	295-550 *non-arm's length income*
specified roll-over amount	Omitted

Current law	*New law*
standard component	295-545(3) *low tax component*
superannuation liability	Omitted
superannuation policy	Omitted
taxable contribution	Omitted
termination of employment	Omitted
unit trust	Omitted
whole of life policy	295-480(1)
267(3)	Omitted
267(4)	Omitted
268	995-1(1) *trustee*
269(2)	295-30
269(3)	Consequential amendments that will be made to subsection 170(10AA) of the ITAA 1936
269A	295-20
269B	Omitted
270	295-5(1)
271	295-15
271A	50-25 item 5.3
272	295-10
273	295-550
273A	295-385(3)
273B	295-390
274(1)(a)(i)	295-160 item 1, 295-165, 295-170
274(1)(a)(ii)	295-190(1) item 2, 295-190(4)
274(1)(aa)	295-160 item 2, 295-165
274(1)(b)(i)	295-190(1) item 1, 295-170(2)
274(1)(b)(ii)	295-160 item 3
274(1)(ba)(i)	295-160 item 1, 295-155, 295-156

Current law	*New law*
274(1)(ba)(ii)	295-190(1) item 2, 295-170(4)
274(1)(ba)(iii)	295-190(1) item 1, 295-170(2), (3)
274(1)(ba)(iv)	295-150 item 3
274(1)(c)	295-190(1) item 2, 295-170(4)
274(1)(d)	295-160 item 3
274(1)(e)	295-160 item 4, 295-156
274(2)	295-190(2), (3)
274(3)	295-190(2), (3)
274(7)	295-180(1), (2)
274(8)	295-180(3)
274(9)	295-180(4)
274(10)(a)	Omitted
274(10)(b)	Omitted
274(10)(c)	295-200
274(10)(d)	295-200
275(2)(a) as it applies to a life insurance company	320-15(1)(i)
275(2)(a) as it applies to a PST	295-320 item 1
275	295-260
275A	295-265(2), (3), (4)
275B	295-265(1), (5), (6), (7), (8)
276(1)	295-490 item 2
276(2)	295-490 item 2
276(3)	295-195(2), (3)
276(4)	295-195(3)
276(5)	Omitted
277	295-95
277AA	295-95
277A	295-490 item 1
278	295-5(2), 4-1

Current law	*New law*
279	295-465
279A	295-320 item 4
279B	295-470
279D(1)(a)(ii)	320-107
279D	295-485
279E	295-100
280	295-495 item 1
281	Subdivision 295-C, Subdivision 295-D
282	Omitted
282A	295-335 item 1
282B	295-385
283	295-390
284	295-545(1), (2)
285	295-545(1), (3)
286	295-5(2), 4-1
286A	295-490 item 4
287	295-495 item 2
288	Subdivision 295-C
288A	295-320 item 2, 295-325
288B	295-320 item 3, 295-330
289	295-5(2), 4-1
289A	295-100
290	Subdivision 295-C, 295-260
291	Omitted
291A	295-335 item 1
292	295-545(1), (2)
293	295-545(1), (3)
294	295-5(2), 4-1
295	Subdivision 295-C
296(1)	295-5(3), 4-1
296(2)	295-105(1), 4-1
297	Omitted

Current law	*New law*
297A	295-335 item 1
297B	295-400
297C	295-335 item 2
298	295-545(1), (2)
299	295-545(1), (3)
299A	295-5(4)
299B	Subdivision 295-C
299C	295-410, 295-540(1), (2)
299CA	295-555(3)
299D(1)	295-555(1)
299D(2)	295-555(2)
299D(3)	295-555(4)
299E(1)	295-475
299E(2)	295-495 item 3
299E(3)	295-495 item 4
299F	295-320 item 5
299G	295-405 items 2 and 3
300(1)(a)	Omitted
300(1)(b)	Omitted
300(2)(a)	Omitted
300(2)(b)	Omitted
300A	295-25
300B	295-270
301	295-30
304	295-85
315A	295-490 item 3
315B	295-490 item 3
315C	295-405 item 1
315D	295-495 item 5
315E	295-490(2)
315F	295-490(3)

Chapter 4
Employment termination payments

Outline of chapter

4.1 Schedule 2 to this Bill establishes the taxation treatment of employment termination payments as a result of the Government's *Simplified Superannuation* reforms.

4.2 Currently, payments made in consequence of the termination of employment are a subset of the existing eligible termination payment (ETP) category of statutory income. ETPs will cease to exist from 1 July 2007, being replaced by employment termination payments and superannuation lump sums (dealt with elsewhere in this Bill). Employment termination payments will cover payments in consequence of termination where such a payment is not made from a superannuation entity.

4.3 Schedule 2 also contains a number of provisions to move associated payments from the *Income Tax Assessment Act 1936* (ITAA 1936) into the *Income Tax Assessment Act 1997* (ITAA 1997). These provisions retain the same effect as under existing law but have been rewritten to reflect the current drafting style and to deliver legislative simplification.

Context of amendments

4.4 Under current legislation, the concessional taxation treatment of ETPs is in line with the taxation arrangements that apply to superannuation benefits, including the application of the reasonable benefit limits (RBLs).

Summary of new law

4.5 The reforms made as part of *Simplified Superannuation* mean that it is no longer appropriate to continue to treat these payments as having a retirement payment characteristic.

4.6 The reforms will remove the current limits on the amount of taxation concessions attached to these payments. The concessionality of the tax treatment of employment termination payments is limited under existing legislation through the operation of RBLs and end benefits tax. The RBLs will be abolished from 1 July 2007 as part of the Government's *Simplified Superannuation* reforms.

4.7 Under *Simplified Superannuation*, employment termination payments received in a given year or relating to a single termination (where the payment is split over more than one year) only receive concessional tax treatment for amounts below the employment termination payments cap. The cap will be $140,000 in 2007-08 and will be indexed. As with the existing law, the Medicare levy is payable in addition to the maximum rate of tax which applies to an employment termination payment.

4.8 To access these tax concessions, employment termination payments must generally be made within 12 months of the employment termination.

4.9 As superannuation benefits paid to those over 60 will be tax free, employment termination payments will no longer be able to be rolled into superannuation. This would have allowed people to put in place arrangements to avoid the intent of the caps on concessional and post-tax contributions.

4.10 Transitional arrangements are available for certain termination payments made as a result of employment entitlements in place before 10 May 2006. Payments made under these arrangements will attract tax concessions designed to broadly mirror existing arrangements, including the ability to roll these amounts into superannuation. To access the transitional arrangements, payments will need to occur prior to 1 July 2012.

4.11 The amendments apply from 1 July 2007 and affect individuals who receive a payment, other than from a superannuation plan, as a result of their employment termination.

Comparison of key features of new law and current law

New law	*Current law*
Employment termination payments must be made within 12 months of the termination of employment or office, unless the Commissioner of Taxation (Commissioner) considers that 12 months is too short in the circumstances. Genuine redundancy payments and early retirement scheme payments are exempt from this requirement. Employment termination payments, with the exception of certain transitional arrangements, will no longer be able to be paid into superannuation.	Payment may be made at any time following the termination of employment or office. Employees can currently elect to have all or part of a payment made into superannuation.
For recipients who reach preservation age in the year a payment is received, the taxable component of an employment termination payment is taxed at 15 per cent for amounts below the employment termination payments cap ($140,000 from 2007-08, and indexed annually) and at the top marginal rate for amounts above the cap. The pre-July 1983 component will be tax free.	For recipients aged 55 (the current preservation age) and over, the post-June 1983 component is taxed at 15 per cent for amounts below the threshold ($135,590 in 2006-07) and 30 per cent for amounts above the threshold up to the RBL. Amounts above the RBL are effectively taxed at the top marginal rate. Five per cent of the pre-July 1983 component is taxed at marginal rates.
For recipients below preservation age, the taxable component of an employment termination payment is taxed at 30 per cent for amounts below the employment termination payments cap and at the top marginal rate for amounts above the cap. The pre-July 1983 component is tax free.	For recipients below age 55, the post-June 1983 component of an ETP is taxed at 30 per cent for amounts below the RBL. Amounts above the RBL are taxed at the top marginal rate. Five per cent of the pre-July 1983 component is taxed at marginal rates.

New law	*Current law*
Death benefit termination payments are tax free up to the employment termination payments cap for dependants. The pre-July 1983 component is tax free. Death benefit termination payments are taxed at a maximum of 30 per cent up to the employment termination payments cap if paid to a non-dependant. The pre-July 1983 component is tax free. In both cases, any amount above the cap is taxed at the top marginal rate.	Death benefit termination payments are tax free up to the RBL for dependants. Death benefit termination payments are taxed at a maximum of 30 per cent up to the RBL if paid to a non-dependant. Five per cent of the pre-July 1983 component is taxed at marginal rates.

* The Medicare levy is payable in addition to the maximum rate.

Detailed explanation of new law

Employment termination payments

4.12 These amendments apply to payments to individuals who retire or stop working provided that the payment is not made from a superannuation plan. These payments are referred to as 'employment termination payments'.

4.13 As with the existing ETP arrangements, the concept of employment has an expanded meaning in the employment termination payment regime such that it includes the holding of an office. ***[Schedule 2, item 1, section 80-5]***

4.14 The circumstances in which a payment can arise in consequence of the termination of employment (and can therefore be an employment termination payment) include dismissal, resignation, retirement and death. ***[Schedule 2, item 1, section 80-10]***

What is an employment termination payment?

4.15 An 'employment termination payment' is a lump sum payment made in consequence of the termination of an individual's employment. ***[Schedule 2, item 1, subsection 82-130(1)]***

4.16 A ***life benefit termination payment*** is an employment termination payment made in consequence of a person's termination of employment, other than as a result of death. ***[Schedule 2, item 1, subparagraph 82-130(1)(a)(i) and subsection 82-130(2)]***

4.17 A ***death benefit termination payment*** is an employment termination payment made to a person after another person's death. ***[Schedule 2, item 1 subparagraph 82-130(1)(a)(ii) and subsection 82-130(3)]***

4.18 To qualify as an employment termination payment, the payment must be made within 12 months of the termination. However, provision is made for the Commissioner to allow a payment made after this period to be taxed under the concessional arrangements applying to employment termination payments. The Commissioner may prepare determinations covering a class of payments or recipients or in respect of an individual taxpayer. ***[Schedule 2, item 1, paragraphs 82-130(1)(b) and 82-130(4)(a) and subsections 82-130(5) to (8)]***

4.19 The 12-month rule exists to prevent abuse of the tax concession offered for these payments by using a series of payments over a number of income years. The provisions dealing with the Commissioner's ability to issue a determination are provided to allow flexibility where delays in payment are reasonable and not constructed with the intent of delivering taxation advantages. The following examples illustrate the circumstances in which it is intended the Commissioner would, or would not, issue such a determination.

Example 4.1

Stephen is dismissed from his employment. No employment termination payment is made. Stephen commences legal action against the employer to secure payment of amounts he believes he was entitled to on termination and to seek damages for unfair dismissal.

After a lengthy court process, lasting more than 12 months, Stephen is successful in his claim and a payment is made by his

employer. Stephen writes to the Commissioner to seek relief from the 12-month rule. The Commissioner, having regard to the circumstances of the payment, determines that the delay in payment is reasonable given that it arose as a result of a legal dispute over entitlement.

Example 4.2

Rachel is employed in a company selling mining hardware. After a period of declining sales, the company suffers financial difficulties out of which it determines that it is unable to trade, and Rachel is dismissed. An administrator is appointed and determines that the company has no cash and must rely on the sale of its assets to meet its outstanding liabilities.

After 18 months all assets of the company are sold and the administrator is ready to make payments to creditors. At this point Rachel receives a payment in respect of the termination of her employment. Rachel writes to the Commissioner to seek relief from the 12-month rule (in so far as the payment is not a genuine redundancy payment and hence exempt from the 12-month rule). The Commissioner, having regard to the circumstances of the person making the payment, determines that the delay in payment is reasonable given that the payment could not be made earlier as a result of the financial situation of the payer.

Example 4.3

Rithy is employed part-time by Erica. They have an agreement which provides for a payment to Rithy on the termination of his employment. Rithy is also employed part-time with Louise. They also have an agreement which provides for a payment on the termination of employment.

On 1 July Rithy terminates his employment with both employers in order to take a holiday. At Rithy's request neither employer makes an immediate payment. On 1 July the following year Louise pays Rithy $140,000. Rithy then enters into an arrangement with Erica to defer the payment of the amount she owes him for another year in order to secure a better taxation outcome.

As the deferral of the payment would mean that it occurs more than 12 months after the termination of employment Rithy seeks the Commissioner's agreement to determine that the 12-month rule does not apply. Given the circumstances of the request and

of the payment the Commissioner declines to provide such a determination.

4.20 Genuine redundancy payments and early retirement scheme payments (including amounts in excess of the tax free component) are exempted from the operation of the 12-month rule. ***[Schedule 2, item 1, paragraph 82-130(4)(b)]***

4.21 Provision is made to ensure that the existing ability to receive an ETP as a transfer of property is retained under the employment termination payments regime. This will also apply to genuine redundancy payments, early retirement scheme payments and foreign termination payments. The value of such a payment is to be assessed as the market value of the property *less* any consideration given for the transfer of the property. ***[Schedule 2, item 1, section 80-15]***

Payments that are not employment termination payments

4.22 Consistent with current legislation, certain payments are prevented from qualifying as employment termination payments. The following payments are expressly stated to not be employment termination payments:

- superannuation benefits;
- payments from a pension or an annuity (to exclude from these provisions an income stream which may be paid by an employer);
- unused annual leave payments;
- unused long service leave payments;
- the part of a genuine redundancy payment or an early retirement scheme payment that is tax free;
- foreign termination payments;
- advances or loans on arm’s length terms;
- a payment that is deemed to be a dividend under paragraph 109(1)(d) of the ITAA 1936;
- reasonable capital payments for personal injury;

- reasonable capital payments for restraint of trade; and
- payments resulting from the commutation of a superannuation income stream that are wholly applied in paying any superannuation contributions surcharge.

[Schedule 2, item 1, paragraph 82-130(1)(c) and section 82-135]

Payments for the individual's benefit or at the individual's direction or request

4.23 Payments to which Divisions 82 and 83 apply are taxed as though they were paid directly to the individual, even if the individual directs their employer to make the payment to another person. However, this does not mean that where a death benefit termination payment is made, that the deceased is assessed as if they had received the payment. ***[Schedule 2, item 1, section 80-20]***

Tax treatment of life benefit termination payments

4.24 The concessionality of the tax treatment of employment termination payments is limited under existing legislation through the operation of RBLs and end benefits tax. The RBLs will be abolished from 1 July 2007 as part of the Government's *Simplified Superannuation* reforms. As a result, new taxation arrangements are required to ensure that certain payments on the termination of employment continue to receive more concessional taxation treatment than other forms of income while preventing abuse of the system.

4.25 Under the new arrangements, an individual who receives an employment termination payment after they reach their preservation age, or in the year in which they will reach their preservation age, will pay less tax on that payment than if it was received by an individual who is below their preservation age for the whole income year in which the payment is received.

4.26 The ***tax free component*** is the portion of an employment termination payment that relates to invalidity or to pre-July 1983 employment. This portion of the payment will not be subject to tax and it will not be exempt income (ie, it is tax free). ***[Schedule 2, item 1, subsection 82-10(1) and section 82-140]***

4.27 An employment termination payment contains an 'invalidity segment' if:

- the payment was made to a person because they can no longer work because of physical or mental ill-health;
- the person stopped working before they reached their 'last retirement day'; and
- two legally qualified medical practitioners have certified that it is unlikely the person can ever work again in a role for which they are qualified by virtue of training, experience or education.

[Schedule 2, item 1, subsection 82-150(1)]

4.28 The ***invalidity segment*** is calculated as the portion of the payment that represents the period between termination and the person's 'last retirement day'. ***[Schedule 2, item 1, subsection 82-150(2)]***

4.29 The pre-July 1983 segment is calculated as the portion of the payment that represents the individual's service period prior to 1 July 1983. The methodology for calculating this is currently set out in the ITAA 1936. The formula to be inserted into the ITAA 1997 effectively mirrors the existing calculation by apportioning the benefit based on the number of days of service prior to 1 July 1983 *divided* by the total number of days in the service period. ***[Schedule 2, item 1, section 82-155]***

4.30 The ***taxable component*** is the part of an employment termination payment that is not the tax free component (ie, the remainder of the payment after the tax free component is calculated). ***[Schedule 2, item 1, section 82-145]***

Treatment of the taxable component

4.31 The taxable component of an employment termination payment is included in an individual's assessable income for tax purposes. ***[Schedule 2, item 1, subsection 82-10(2)]***

4.32 Individuals who have reached their preservation age (or will do so in the income year in which they receive the payment) will pay no more than 15 per cent tax on the taxable component of the employment termination payment that is within the

employment termination payments cap. ***[Schedule 2, item 1, paragraph 82-10(3)(a) and subsection 82-10(4)]***

4.33 Individuals who are below their preservation age throughout an income year will pay no more than 30 per cent tax on the taxable component of the employment termination payment that is within the employment termination payments cap. ***[Schedule 2, item 1, paragraph 82-10(3)(b) and subsection 82-10(4)]***

4.34 The ***employment termination payments cap*** for the 2007-08 financial year is $140,000. The amount of the cap will be indexed annually. Details of the indexation arrangements can be found in Chapter 7 of this explanatory memorandum. ***[Schedule 2, item 1, section 82-160]***

4.35 If the employment termination payment is greater than the employment termination payments cap, the amount above the cap will be taxed at the top marginal rate in accordance with the *Income Tax Rates Act 1986*.

Example 4.4

> In November 2007, Ryan retires from his position as an executive at Mighty Power at age 65 after working there for 20 years. He receives a payment of $400,000 as a retirement bonus. As the payment relates only to post-June 1983 employment and there is no invalidity segment, there is no tax free component. Ryan pays tax at no more than 15 per cent on the first $140,000 of the payment and at the top marginal rate on the remaining $260,000.

4.36 The employment termination payments cap is reduced by the amount of any earlier life benefit termination payment received in the same financial year. This means that if the cap is exceeded by an earlier employment termination payment, any further payments received in the same year will be taxed at the top marginal rate. ***[Schedule 2, item 1, paragraph 82-10(4)(a)]***

Example 4.5

> Continuing Example 4.4, following his retirement, Ryan is approached to undertake a consulting role due to his industry experience. The consultancy is undertaken over a six month period and as part of his contract he receives a $100,000 payment when the work is complete. The payment falls within the same income year as his retirement from Mighty Power. As

> the employment termination payments cap was exceeded by the payment from Mighty Power, Ryan will pay tax at the top marginal rate on the full amount of the second employment termination payment.

4.37 The employment termination payments cap is also reduced by any earlier payments (whether in the same income year, or previous income years) received in relation to the same termination. This will mean that no more than the employment termination payments cap amount ($140,000 in 2007-08) can be received at concessional taxation rates in respect of any one termination. This ensures that individuals can not seek to pay less tax by having their employment termination payment paid to them in instalments over two or more years. ***[Schedule 2, item 1 , paragraph 82-10(4)(b)]***

Example 4.6

> Ryan, having terminated his employment with Mighty Power and being entitled to receive an employment termination payment of $400,000, arranges for his employer to make a payment of $200,000 in the income year in which his employment was terminated. He has no other employment termination payments in that year. The first $140,000 is taxed at no more than 15 per cent (as Ryan is 65). The remaining $60,000 is taxed at the top marginal rate.
>
> The remainder of Ryan's entitlement is paid to him in the following income year. The available taxation concession for Ryan in the second income year is reduced by the $140,000 he received at concessional tax rates in the earlier income year. Assuming no increase in the value of the employment termination payments cap, the entirety of the $200,000 received in the subsequent income year would be taxed at the top marginal rate.

Termination payments made more than 12 months after termination

4.38 A payment that would have been an employment termination payment, had it been made within 12 months of the employment termination, is assessable income and subject to tax at an individual's marginal tax rate if it is paid after the 12-month period and is not exempted from the 12-month rule by a determination by the Commissioner. ***[Schedule 2, item 1, section 83-295]***

Death benefit termination payments

4.39 The amendments apply to death benefit termination payments from 1 July 2007. Changes to the tax treatment of these payments reflect the abolition of benefits tax and RBLs, which operate to limit the concessional tax treatment of death benefit payments under existing legislation.

4.40 The tax treatment of death benefit termination payments depends on whether the recipient was a death benefits dependant of the deceased.

Death benefit termination payments to dependants

4.41 Any tax free component of an employment termination payment received by a death benefits dependant is not subject to tax. ***[Schedule 2, item 1, subsection 82-65(1)]***

4.42 The part of the taxable component of a death benefit termination payment that is within the employment termination payments cap is not subject to tax and is not exempt income (ie, it is tax free) when paid to a death benefits dependant. ***[Schedule 2, item 1, paragraph 82-65(2)(a) and subsection 82-65(3)]***

4.43 The part of the taxable component of a death benefit termination payment that exceeds the employment termination payments cap will be taxed at the top marginal rate. ***[Schedule 2, item 1, paragraph 82-65(2)(b) and subsection 82-65(3)]***

4.44 As with life benefit termination payments, the employment termination payments cap is reduced by any death benefit termination payments received in the same or previous financial years in consequence of the same termination of employment. ***[Schedule 2, item 1, subsection 82-65(4)]***

Example 4.7

Angela is a full-time student who lives at home. Her mother, who has supported her throughout her studies, dies. Her mother's employer pays Angela a death benefit termination payment of $150,000. As Angela was a death benefits dependant, she will pay no tax on the first $140,000 of the payment. She will pay tax at the top marginal rate on the remaining $10,000.

Death benefit termination payments for non-dependants

4.45 Death benefit termination payments made to those who are not death benefits dependants (non-dependants) will be taxed less concessionally than payments made to death benefits dependants. The additional concession available to death benefits dependants reflects the reliance these people had on the income of the deceased.

4.46 Any tax free component of an employment termination payment received by the non-dependant is not subject to tax. ***[Schedule 2, item 1, subsection 82-70(1)]***

4.47 The remaining portion of a death benefit termination payment – the taxable component – is taxed at a maximum rate of 30 per cent for amounts below the employment termination payments cap. Any part of the payment that exceeds the employment termination payments cap is taxed at the top marginal rate. ***[Schedule 2, item 1, subsections 82-70(2) to (4)]***

Example 4.8

> Mark is employed full-time as a carpenter. Following the death of his grandfather, he receives a death benefit termination payment of $200,000 from his grandfather's employer. The pre-July 1983 component of this payment is $75,000. This amount is the tax free component and is not subject to tax. The remaining $125,000 is the taxable component, and as Mark was not a death benefits dependant of his grandfather, Mark will pay tax at no more than 30 per cent on this amount.

4.48 As with life benefit termination payments, the employment termination payments cap is reduced by any death benefit termination payments received in the same or previous financial years in consequence of the same termination of employment. ***[Schedule 2, item 1, subsection 82-70(5)]***

Death benefits paid to the trustee of a deceased estate

4.49 Death benefit termination payments to trustees of deceased estates are subject to slightly different treatment than payments made directly to beneficiaries. ***[Schedule 2, item 1, subsections 82-65(5), 70(6) and 75(1)]***

4.50 The portions of a death benefit termination payment relating to beneficiaries will be taxed in the hands of the trustee in the same way it would have been taxed if paid directly to a beneficiary.

4.51 The proportion of a payment that has or will benefit death benefits dependants of the deceased will be subject to tax as if the trustee of the deceased estate was a death benefits dependant who received the payment. ***[Schedule 2, item 1, subsection 82-75(2)]***

4.52 The proportion of a payment that has or will benefit non-dependants of the deceased will be subject to tax as if the trustee of the deceased estate was a non-dependant who received the payment. ***[Schedule 2, item 1, subsection 82-75(3)]***

Example 4.9

Yasmin is the trustee of her friend Michael's estate. Michael's will evenly divided his estate between his daughter and nephew. Michael's nephew is not a death benefits dependant, but his daughter is a death benefits dependant. As trustee, Yasmin receives a death benefit termination payment from Michael's employer of $150,000 (of which there is no tax free component). Half of the payment will be treated as though it had been paid directly to Michael's daughter and will not be subject to tax. The remaining $75,000 will be treated as though it had been paid directly to Michael's nephew and will be subject to tax at 30 per cent as it is below the employment termination payments cap.

Example 4.10

Matthew is the trustee of his friend Justin's estate. Justin's will evenly divided his estate between his son, Ricky, who is a death benefits dependant, and his three friends, Glenn, Shane and Adam. As trustee, Matthew receives a death benefit termination payment from Justin's employer of $400,000 (of which there is no tax free component). One quarter of the payment ($100,000) will be treated as though it had been paid directly to Justin's son Ricky. As this amount is less than $140,000 it will not be subject to tax. The remaining $300,000 will be treated as if it were paid to Matthew as a non-dependant of Justin. The first $140,000 of this amount will be taxed at 30 per cent. The remaining $160,000 will be taxed at the top marginal tax rate.

Other payments on termination

4.53 Division 83 of the ITAA 1997 contains the provisions related to unused annual leave, unused long service leave, genuine redundancy payments, early retirement scheme payments and foreign termination payments. The provisions relating to these payments are intended to retain their existing application but may have been redrafted to reflect current drafting approaches.

Unused annual leave payments

4.54 A person's assessable income will continue to include payments in consequence of unused annual leave, recreational leave, annual holidays and any other similar leave. ***[Schedule 2, item 1, subsections 83-10(1) and (2)]***

4.55 An ***unused annual leave payment*** is a payment or bonus in relation to unused annual leave (including for leave that is yet to accrue) in consequence of an employment termination. ***[Schedule 2, item 1 , subsection 83-10(3)]***

4.56 To the extent that an unused annual leave payment is made in connection with a genuine redundancy payment, early retirement scheme payment, the individual's invalidity or relates to employment before 18 August 1993 the rate of tax will be no more than 30 per cent (plus the Medicare levy). These eligibility criteria are the same as under existing legislation. Any other unused annual leave payments are taxed at marginal rates. ***[Schedule 2, item 1, section 83-15]***

Unused long service leave payments

4.57 A person's assessable income will continue to include payments in consequence of unused long service leave that are paid in consequence of an employment termination. The definition of 'unused long service leave' and the criteria for entitlement to a tax offset (including the methodology for calculating the components attributable to different periods and to part-time and full-time work) are the same as under existing legislation. ***[Schedule 2, item 1, sections 83-70 to 83-115]***

Genuine redundancy payments and early retirement scheme payments

4.58 The new terminology of 'genuine redundancy payment' and 'early retirement scheme payment' replace the existing ITAA 1936 terminology dealing with payments in consequence of bona fide redundancy and approved early retirement schemes respectively. ***[Schedule 2, item 1, subsection 83-170(1) and sections 83-175 and 83-180]***

Tax treatment

4.59 Genuine redundancy payments and early retirement scheme payments continue to receive the same concessional tax treatment provided for in the ITAA 1936.

4.60 The tax free part of the payment is excluded from assessable income and is not exempt income. ***[Schedule 2, item 1, subsection 83-170(2)]***

4.61 The tax free part of a payment is determined by reference to a base amount plus an amount per year of service. This replicates the existing concession offered to such payments. ***[Schedule 2, item 1, subsection 83-170(3)]***

4.62 If a payment on redundancy or early retirement exceeds the available tax free amount then the remaining part of the payment will qualify as an employment termination payment and be taxed accordingly. ***[Schedule 2, item 1, subsections 83-175(4) and 180(6) and section 82-130]***

Foreign termination payments

4.63 Termination payments related exclusively to overseas employment or service are treated differently to employment termination payments resulting from domestic employment.

4.64 The treatment of these payments reflects the existing treatment of exempt non-resident foreign termination payments and exempt resident termination payments as contained in the ITAA 1936. Payments that meet the conditions in sections 83-235 and 83-240 are not subject to tax in the hands of the recipient (ie, they are not assessable). They are, however, not exempt income. ***[Schedule 2, item 1, Subdivision 83-D]***

Application provisions

4.65 These amendments apply from 1 July 2007.

Transitional provisions

Pre-10 May 2006 entitlement to a termination payment

4.66 The transitional provisions operate to reduce the risk that employees with an entitlement to a payment on termination as at 9 May 2006 will terminate employment prior to that date in order to access the existing ETP provisions, including the ability to have an unlimited amount of such a payment made to a superannuation fund.

4.67 The transitional arrangements apply where a person is entitled, as at 9 May 2006, to a payment on termination of employment under a written contract, Australian or foreign law, legal instrument or workplace agreement made under the *Workplace Relations Act 1996*, provided that the payment is made before 1 July 2012. Such a payment is referred to as a 'transitional termination payment'. Payments to which these transitional arrangements apply are not taxed under the normal employment termination payment provisions in the ITAA 1997. ***[Schedule 2, item 2, subsections 82-10(1), (2), (5) and (6)]***

4.68 In order to ensure that the transitional provisions are not open to abuse, they are only available in situations where the payment was able to be determined as at 9 May 2006. This will encompass arrangements where the contract refers to the amount of the payment by way of a formula which can be objectively determined, or to payments made in kind (eg, shares). ***[Schedule 2, item 2, subsections 82-10(3) and (4)]***

Example 4.11

Duncan is to have his employment terminated shortly after 1 July 2007. If Duncan were entitled, as at 9 May 2006, to an amount of $10,000 or an amount of 10,000 shares in the company, this would meet the transitional provision requirement of being a specified amount or providing for a way to work out the amount. If Duncan were able to choose between the shares or the cash, or was entitled to whichever had the

greater value at termination, this would also meet the requirements. If Duncan were entitled to 10,000 shares only if they were at the time worth more than $5 each, this would also satisfy the test.

If the payer has discretion as to whether the payment is made (but not the value of the payment) then such payments are also likely to satisfy the transitional provisions. For instance, if Duncan was entitled to 10,000 shares of the company if, in the opinion of the Board, he has raised the value of the company, or if he was entitled to $10,000 or 10,000 shares at the Board's discretion, these payments would qualify for the transitional arrangements. This is because the amount of the payment is still specified or able to be determined, despite the fact that the Board holds the sole decision-making power about the payment.

If Duncan was entitled to an amount of money, or number of shares, at the complete discretion of the Board, this would not meet the requirements of the transitional provisions. Similarly, if the Board was to determine the value of the payment as an amount equal to 10 per cent of the amount by which the Board considers that Duncan has raised the value of the company, this would also fail to meet the requirements.

Taxation treatment if the recipient is below preservation age

4.69 The tax free component of a transitional termination payment made to a person below preservation age is not subject to tax. ***[Schedule 2, item 2, subsection 82-10C(2)]***

4.70 Any remaining part of the payment — the taxable component — is included in assessable income. ***[Schedule 2, item 2, subsection 82-10C(3)]***

4.71 The amount of the taxable component that does not exceed the upper cap amount of $1 million will be taxed at no more than 30 per cent. ***[Schedule 2, item 2, subsections 82-10C(3) to (5)]***

4.72 The upper cap amount of $1 million is the upper limit on the amount of concessions that may be received during the transitional period. Therefore, the taxable components of *all* previous transitional termination payments, including directed termination payments, reduce the upper cap amount. ***[Schedule 2, item 2, section 82-10D]***

4.73 Any amount which exceeds the upper cap amount worked out under section 82-10D is taxed at the top marginal rate.

Taxation treatment if the recipient has reached preservation age

4.74 If the recipient of a transitional termination payment will reach preservation age by the end of the income year in which the payment is received, the tax free component of the payment is not subject to tax. ***[Schedule 2, item 2, subsections 82-10A(1) and (2)]***

4.75 The taxable component of a transitional termination payment is included in assessable income. ***[Schedule 2, item 2, subsection 82-10A(3)]***

4.76 The amount of any transitional termination payment that does not exceed the 'lower cap amount' will be taxed at no more than 15 per cent. ***[Schedule 2, item 2, subsections 82-10A(4) and (6) and section 82-10B]***

4.77 The amount of a transitional payment that exceeds the lower cap amount but does not exceed the upper cap amount will be taxed at no more than 30 per cent Any amount in excess of the upper cap will be taxed at the top marginal rate in accordance with the *Income Tax Rates Act 1986*. ***[Schedule 2, item 2, subsections 82-10A(5) and (7)]***

Example 4.12

> Lian retires on 1 January 2008 at the age of 55. As at 9 May 2006 Lian was entitled to receive a payment on termination of $1.5 million. Lian will pay tax on the payment at a rate of no more than 15 per cent on the first $140,000, at a rate of no more than 30 per cent on the next $860,000 and at the top marginal tax rate on the remaining $500,000.

4.78 The lower and upper caps apply to each individual for the duration of the transitional period. Accordingly, the caps are reduced by the taxable components of any earlier transitional termination payments they may have received, including directed termination payments. ***[Schedule 2, item 2, sections 82-10B and 82-10D]***

4.79 The lower cap amount is reduced by all amounts that have previously used the concession available to amounts below the lower cap amount. In addition, the lower cap amount is also reduced if the total of the taxable components of all directed

termination payments in the income year in which the recipient reached preservation age or later and the taxable components of all payments received before preservation age exceed the difference between the upper cap amount and the lower cap amount. This prevents an individual, for example, receiving $900,000 worth of concessions before they reach preservation age, and an extra $140,000 of concessions after they reach preservation age, exceeding the concessional limit of $1 million (see Example 4.13). The lower cap amount cross-references the value of the employment termination payments cap and as such will be subject to indexation as that cap is indexed. ***[Schedule 2, item 2, section 82-10B]***

4.80 The upper cap amount is reduced by the taxable components of all previous transitional payments, including directed termination payments. ***[Schedule 2, item 2, section 82-10D]***

4.81 Any amount above the upper cap amount is taxed at the top marginal rate.

Example 4.13

Lian is the managing director of the Bouncing Baby child-care agency. Under the terms of her contract as at 9 May 2006, she is entitled to a termination payment of $900,000. She is also employed by Max's Employment Agency, and under her contract as at 9 May 2006 she is entitled to a payment of $500,000 on termination.

On 1 July 2008, on her 54th birthday, Lian retires from her role with Bouncing Baby, and receives her transitional termination payment of $900,000. On 1 July 2009 on her 55th birthday, she retires from Max's Employment Agency and receives a payment of $500,000.

None of the payments have a tax free component.

First payment

For the 2008-09 income year, Lian's entire payment of $900,000 will be taxed at no more than 30 per cent, because she is under her preservation age for the entire year and the payment does not exceed the upper cap amount of $1 million (subsections 82-10C(1) and (3) to (5)).

Second payment

The taxation of Lian's payment in the 2009-10 financial year is affected by the payment she received in the previous year, which will have to be taken into account when determining the tax rate on her second payment.

As this second payment is made in the year in which Lian turned 55, she may be entitled to have an amount taxed at no more than 15 per cent. This amount is called the 'low rate part' and is that part of the payment which does not exceed the lower cap amount (subsection 82-10A(4)).

The formula in subsection 82-10B(2) reduces the lower cap amount by an amount called the 'cap excess' and all previous transitional payments which have been taxed at 15 per cent.

The 'cap excess' is the amount by which the sum of all previous transitional termination payments received prior to preservation age (plus any directed termination payments made after preservation age but prior to the payment in question) exceeds the 'cap difference' (subsection 82-10B(3)).

The 'cap difference' is determined by subtracting the employment termination payments cap from $1 million (subsection 82-10B(3), step 3 of the method statement).

Assuming no indexation, this gives the following result:

$1,000,000 – $140,000 = $860,000

In this example, the only earlier payment was the $900,000 Lian received on 1 July 2008. The cap excess is the amount by which this payment exceeds the cap difference. This is worked out under subsection 82-10B(3), step 3 of the method statement which gives the following result:

$900,000 – $860,000 = $40,000

This reduces the lower cap amount to $100,000. Lian's low rate part is therefore $100,000 which is taxed at a maximum rate of 15 per cent (subsections 82-10A(4) and (6)).

The 'middle rate' part is so much of Lian's second payment that exceeds her low rate part, but does not exceed the amount worked out as:

Upper cap amount – lower cap amount

As Lian's upper cap amount has been reduced by the $900,000 she previously received, the following calculation applies:

$100,000 (the reduced upper cap amount) – $100,000 (the lower cap amount reduced by the cap excess) = $0 (subsections 82-10A(5) and (7)).

Therefore none of the remaining $400,000 of Lian's second payment is entitled to concessional taxation treatment. $400,000 of Lian's second payment will be taxed at the top marginal tax rate.

Pre-payment statements

4.82 Employers who propose to pay a transitional termination payment are required to provide an individual with a 'pre-payment statement'. The statement must outline the components of the proposed payment and must ask the individual to make a choice between receiving the payment themselves, or a 'directed termination payment'. ***[Schedule 2, item 2, section 82-10E]***

Transitional termination payment choice

4.83 An individual who wants to make a choice must advise their employer of their payment choice (ie, a direct payment to the individual or a directed termination payment) in the approved form and within 30 days of receipt of a pre-payment statement. In the absence of a decision, the payment must be made directly to the individual. ***[Schedule 2, item 2, section 82-10F]***

4.84 A ***directed termination payment*** is a payment that an individual directs the payer to make to a complying superannuation plan or to purchase a superannuation annuity. ***[Schedule 2, item 2, subsection 82-10F(1) and paragraphs 82-10F(2)(a) and (b)]***

4.85 If the recipient chooses to have the payer make a directed termination payment, the payer must comply with the direction and must give the recipient of the payment the details of the components of the payment. ***[Schedule 2, item 2, paragraphs 82-10F(4)(a) and (b)]***

Taxation of directed termination payments

4.86 A directed termination payment is not subject to income tax and is not exempt income for the individual. The payment may be included in the assessable income of the superannuation provider. ***[Schedule 2, item 2, section 82-10G]***

Pre-10 May 2006 entitlements: payments made after 1 July 2012

4.87 The employment termination payments cap applying to payments made after 1 July 2012 will be reduced by the amount of any transitional termination payments relating to the same employment termination, whether the transitional payment was made directly to the individual or rolled over into superannuation. ***[Schedule 2, item 2, section 82-10H]***

Failure to make a transitional payment as directed

4.88 Amendments are being made to the *Taxation Administration Act 1953* to apply penalties to transitional termination payment payers who receive a choice under subsection 82-10F(5) and do not make the payment as directed. ***[Schedule 2, items 3 and 4, paragraphs 8C(1)(h) and (i)]***

Chapter 5
Social security arrangements

Outline of chapter

5.1 Schedules 8 and 9 to this Bill amend the *Social Security Act 1991* and the *Veterans' Entitlements Act 1986* respectively to implement changes to the assets-test to:

- halve the pension assets-test taper rate from $3 to $1.50 per fortnight for every $1,000 of assets over the free area, with effect from 20 September 2007; and
- remove the 50 per cent assets-test exemption for complying income streams purchased on or after 20 September 2007.

5.2 The Schedules also contain minor consequential amendments on income stream products to the *Social Security Act 1991* and the *Veterans' Entitlements Act 1986*.

Context of amendments

5.3 Currently, recipients of the age pension, disability support pension, carer payment, bereavement allowance, wife pension, widow B pension, service pension and income support supplement lose $3 per fortnight for every $1,000 of assets above the relevant threshold (currently $161,500 for single homeowners, and $229,000 for couple homeowners – for non-homeowners these amounts are $278,500 for singles and $346,000 for couples). The effect of the current assets-test taper rate means, for example, that retirees need to achieve a return of at least 7.8 per cent on their additional savings in order to overcome the effect of a reduction in their pension amount.

5.4 Lifetime, life expectancy and market-linked income streams under sections 9A, 9B and 9BA of the *Social Security Act 1991* and sections 5JA, 5JB and 5JBA of the *Veterans' Entitlements*

Act 1986 are currently 'assets-test exempt' for the purposes of the means test. This means that part or all of the asset value of the income stream is not taken into account when determining a person's eligibility for a social security payment.

Summary of new law

Halving of assets-test taper rate

5.5 The amendments in these Schedules halve the assets-test taper rate to $1.50 per fortnight with effect from 20 September 2007, resulting in an increase in the amount of assets a person can hold before being precluded from receiving the age pension, disability support pension, carer payment, bereavement allowance, wife pension, widow B pension, service pension and income support supplement.

5.6 The reduction in the assets-test taper rate will increase incentives to save and boost the retirement incomes of pensioners whose rate of payment is determined by the assets-test. It will also increase the number of people who are eligible for a part pension and the associated concessions.

Changes to the assets-test exemption for income streams

5.7 The amendments in both Schedules give effect to the removal of the assets-test exemption for complying income streams purchased on or after 20 September 2007.

5.8 Retaining the assets-test exemption for 'purchased' income streams alongside the reduced assets-test taper rate would create scope for wealthier individuals to access the pension. The assets-test treatment of income stream products purchased before 20 September 2007 will not change.

5.9 The Schedules also contain provisions for minor consequential amendments to the *Social Security Act 1991* and *Veterans' Entitlements Act 1986* affecting income stream products.

Transitional rules

5.10 Both Schedules contain transitional rules allowing backdating of pension claims made in the three months after the implementation of the assets-test changes on 20 September 2007. These claims can be granted from 20 September 2007 if all eligibility conditions were met from that date. This gives people newly eligible for a pension the safeguard that they have three months to make their claim and can still be paid from 20 September 2007. The purpose of these rules is to reduce the concentration of claims made on or soon after 20 September 2007 and the risk of claim processing delays.

Comparison of key features of new law and current law

New law	*Current law*
Pension assets-test	
Pension recipients only lose $1.50 per fortnight for every $1,000 of assets above the relevant threshold.	Pension recipients lose $3 per fortnight for every $1,000 of assets above the relevant threshold.
Assets-test exemption	
Complying income streams which are purchased before 20 September 2004 are eligible for a full assets-test exemption. Complying income streams purchased from 20 September 2004 and before 20 September 2007 are eligible for a 50 per cent exemption. No exemption from the assets-test for income stream products purchased from 20 September 2007.	Complying income streams which are purchased before 20 September 2004 are eligible for a full assets-test exemption. Complying income streams purchased on or after this date are eligible for a 50 per cent exemption.

Detailed explanation of new law

Schedule 8 — *Social Security Act 1991*

5.11 Schedule 8 amends the *Social Security Act 1991*.

Part 1 — Amendments commencing 20 September 2007

5.12 Item 1 amends section 9A so that income streams purchased or acquired on or after 20 September 2007 (other than defined benefit income streams) will no longer be assets-test exempt. ***[Schedule 8, item 1]***

5.13 Item 2 inserts new subsection 9A(1AA), which has the effect that defined benefit income streams will continue to attract the 100 per cent assets-test exemption, even if they were acquired on or after 20 September 2007. ***[Schedule 8, item 2]***

5.14 Item 3 removes part of subsection 9A(5), which currently gives the Secretary the power to determine that an income stream that does not meet the requirements of subsection 9A(2) is an assets-test exempt income stream. This amendment allows the Secretary to determine that a specific income stream is an assets-test exempt income stream even if it does not meet the requirements of subsection 9A(2). For example, a determination could be made that an existing lifetime assets-test exempt income stream which was created from the commutation and roll-over of an assets-test exempt income stream *purchased* or acquired before 20 September 2007, is also an assets-test exempt income stream provided it retains the features of the original income stream. In addition, another determination may be made that a defined benefit income stream that is acquired from 20 September 2007 is an assets-test exempt income stream. ***[Schedule 8, item 3]***

5.15 Item 4 inserts subsection 9A(5A) to make it clear that a determination made under subsection 9A(5) will apply to the income stream regardless of the commencement date of that income stream. ***[Schedule 8, item 4]***

5.16 Subsection 9A(5B) is inserted to assist readers, as the determination made under subsection 9A(5) is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*. A determination under subsection 9A(5) is

not legislative in character and, accordingly, subsection 9A(5B) is merely declaratory of the law. ***[Schedule 8, item 4]***

5.17 Item 5 repeals subsection 9B(1) and inserts a replacement provision. This new subsection provides that income streams falling within section 9B will no longer be assets-test exempt if purchased or acquired on or after 20 September 2007 unless the Secretary makes a determination about the income stream. ***[Schedule 8, item 5]***

5.18 Item 6 removes part of subsection 9B(4), which currently gives the Secretary the power to determine that an income stream that does not meet the requirements of subsection 9B(2) is an assets-test exempt income stream. This amendment allows the Secretary to determine that a specific income stream is an assets-test exempt income stream even if it does meet the requirements of subsection 9B(2). For example, it would allow a determination that an income stream created on or after 20 September 2007 from the commutation and roll-over of an assets-test exempt life expectancy income stream purchased before 20 September 2007 will retain the assets-test exemption provided it retains the features of the original income stream. ***[Schedule 8, item 6]***

5.19 Item 7 inserts subsection 9B(4A) to make it clear that a determination made under subsection 9B(4) will apply to the income stream regardless of the commencement date of that income stream. ***[Schedule 8, item 7]***

5.20 Subsection 9B(4B) is inserted to assist readers, as the determination made under subsection 9B(4) is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*. A determination under subsection 9B(4) is not legislative in character and, accordingly, subsection 9B(4B) is merely declaratory of the law. ***[Schedule 8, item 7]***

5.21 Item 8 changes the date in subparagraph 9BA(1)(a)(i) so that a market-linked income stream must have been purchased between 20 September 2004 and 19 September 2007 inclusive if it is to receive a 50 per cent exemption under the assets-test. Income streams that arise on or after 20 September 2007 from the commutation and roll-over of a market-linked income stream will only retain the 50 per cent exemption if the Secretary makes a determination about the new income stream. ***[Schedule 8, item 8]***

5.22 Item 9 removes part of subsection 9BA(11), which currently gives the Secretary the power to determine that an income stream that does not meet the requirements of subsection 9BA(2) is an assets-test exempt income stream. This amendment allows the Secretary to determine that a specific income stream is an assets-test exempt income stream even if it does not meet the requirements of subsection 9BA(11). For example, it would allow a determination that an income stream created on or after 20 September 2007 from the commutation and roll-over of an assets-test exempt market-linked income stream purchased before 20 September 2007 will retain the assets-test exemption provided it retains the features of the original income stream. ***[Schedule 8, item 9]***

5.23 Item 10 inserts subsection 9BA(11A) to make it clear that a determination made under subsection 9BA(11) will apply to the income stream regardless of the commencement date of that income stream. ***[Schedule 8, item 10]***

5.24 Subsection 9BA(11B) is inserted to assist readers, as the determination made under subsection 9BA(11) is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*. A determination under subsection 9BA(11) is not legislative in character and, accordingly, subsection 9BA(11B) is merely declaratory of the law. ***[Schedule 8, item 10]***

5.25 Items 11 to 17 repeal the current formula for determining the assets-test taper rate of $3 per fortnight and substitute a formula which will have the effect of halving the taper rate to $1.50 per fortnight. ***[Schedule 8, items 11 to 17]***

5.26 Item 18 repeals the definition of 'partially assets-test exempt income stream' under subsection 1118(1A) and inserts a replacement provision. Paragraph (a) of the new definition in subsection 1118(1A) specifies that a ***partially assets-test exempt income stream*** is an assets-test exempt income stream that:

- is a market-linked income stream (covered by subsection 9BA(1)) or an 'assets-test exempt income stream' (covered by subsection 9A(1) or 9B(1)) that is not in either case a defined benefit income stream;
- commences between 20 September 2004 and 19 September 2007 inclusive; and

- is not covered by principles that the Secretary has determined in relation to this issue.

[Schedule 8, item 18]

5.27 The principles determined by the Secretary in relation to paragraph (a), and specified in a legislative instrument, will cover certain 100 per cent assets-test exempt income streams covered by subsections 9A(1), 9A(1A) and 9B(1) that were purchased or acquired before 20 September 2004, and that are commuted and rolled over to another income stream covered by those provisions. ***[Schedule 8, item 18]***

5.28 If the new income stream is created between 20 September 2004 and 19 September 2007 inclusive, and the income stream is covered by the Secretary's principles, the new income stream will retain the 100 per cent exemption that applied to the original income stream, provided it retains the features of the original income stream. The effect of not being covered by these principles is that these income streams will lose the 100 per cent exemption and only be entitled to a 50 per cent exemption, even if they retain the features of the original income stream. ***[Schedule 8, item 18]***

5.29 If the new income stream covered by subsections 9A(1), 9A(1A) and 9B(1) is subsequently commuted and rolled over to another new income stream covered by subsections 9A(1), 9A(1A) and 9B(1) on or after 20 September 2007, and this new income stream is covered by the Secretary's principles, the new income stream will retain the 100 per cent exemption that applied to the original income stream, provided it retains the features of the original income stream. The effect of not being covered by these principles is that the income streams will lose the 100 per cent exemption altogether, even if they retain the features of the original income stream. ***[Schedule 8, item 18]***

5.30 Paragraph (b) of the new definition in subsection 1118(1A) refers to an income stream that:

- commences on or after 20 September 2007; and
- is covered by principles that the Secretary has determined in relation to this issue.

[Schedule 8, item 18]

5.31 The principles determined by the Secretary in relation to paragraph (b), and specified in a legislative instrument, will cover certain assets-test exempt income streams that do not arise from previously commuted assets-test exempt income streams. These income streams will have been purchased or acquired between 20 September 2004 and 19 September 2007 inclusive, then commuted and rolled over to purchase another income stream that satisfies the requirements of subsections 9A(1), 9A(1A), and 9B(1) and subsection 9BA(1). These income streams will be allowed to retain the 50 per cent exemption from the assets-test in certain circumstances specified in the legislative instrument. ***[Schedule 8, item 18]***

5.32 Item 19 amends the assets-test hardship rules. Currently these rules incorporate a reduction for assets that are not unrealisable based on the existing assets-test taper rate. Item 19 brings this reduction amount into line with the reduction in the assets-test taper rate. ***[Schedule 8, item 19]***

5.33 Item 20 provides transitional rules.

5.34 Subitem 20(1) provides that, where a person makes a claim for a relevant social security payment during the ***claim period*** (defined in subitem 20(3) as the period commencing on 20 September 2007 and ending on 20 December 2007), the person's start day is the earlier of either:

- 20 September 2007, or the day on which the relevant social security payment first becomes payable to the person (whichever is the later); and
- the day worked out under the current start day rules in Schedule 2 to the *Social Security (Administration) Act 1999*.

[Schedule 8, item 20]

5.35 Subitem 20(2) inserts a special rule for a person who makes a claim for a relevant social security payment during the claim period (ie, from 20 September 2007 to 20 December 2007 inclusive) but, on the day on which the claim was made, either the person was not qualified for the relevant payment or the relevant payment was not payable. If the person was qualified for a relevant payment, and the relevant payment was payable, during a period that falls before the day on which the claim was made (the relevant period), which is within the claim period, then the Secretary may grant the claim. The person's start date in relation to the relevant social security payment is the earlier of the first day of the relevant period and the day worked out under the current start day rules in Schedule 2 to the *Social Security Administration Act 1999*. ***[Schedule 8, item 20]***

5.36 Subitem 20(3) defines the term ***claim period*** to mean the period commencing on 20 September 2007 and ending on 20 December 2007 inclusive. The term ***relevant social security payment*** means an age pension, a disability support pension, a wife pension, a carer payment, a widow B pension or a bereavement allowance. ***[Schedule 8, item 20]***

Part 2 — Amendment commencing 1 July 2007

5.37 Part 2 contains an amendment to insert a new definition of 'deductible amount'. The amendment will commence on 1 July 2007.

5.38 Item 21 repeals and replaces the definition of 'deductible amount' at subsection 9(1). ***[Schedule 8, item 21]***

5.39 Under the social security legislation, the 'deductible amount' is used to determine assessable income for defined benefit income streams (as defined in subsection 9(1F) of the *Social Security Act 1991*) but not for 'purchased' income streams. The social security definition refers to the definition of 'deductible amount' in the *Income Tax Assessment Act 1936* (ITAA 1936) which is used to determine assessable income for tax purposes. ***[Schedule 8, item 21]***

5.40 Defined benefit income streams are lifetime income streams where the payments are not fully determined in relation to a particular sum of money used to acquire the income stream but also by other factors, for example, completed years of service and the retiree's salary in the years immediately preceding retirement.

Under the income test, assessable income for these income streams is determined by reducing their gross annual income by the deductible amount. Currently the value of the deductible amount remains constant throughout the life of the income stream. ***[Schedule 8, item 21]***

5.41 The amendments that will apply to the *Income Tax Assessment Act 1997* (ITAA 1997) from 1 July 2007, will move the tax treatment of superannuation income stream benefits from an annual basis to a *per payment* basis. As a result, the annual deductible amount needs to be converted into a *per benefit* (ie, per payment) figure to maintain the existing tax treatment (see subsection 307-125(2) of the *Income Tax (Transitional Provisions) Act 1997*). ***[Schedule 8, item 21]***

5.42 This will be achieved by apportioning the annual deductible amount across each superannuation income stream according to the value of each of the superannuation income stream benefits received in the income year. The portion of the deductible amount applying to a particular superannuation income stream benefit will be the 'tax free component' for that superannuation income stream benefit (see subsection 307-125(2) of the *Income Tax (Transitional Provisions) Act 1997)*. The 'tax free component' is paid 'tax free' to the recipient, and comprises several segments that are specified in this Bill. ***[Schedule 8, item 21]***

5.43 Under the new arrangements, the value of the 'tax free component' of a superannuation interest is worked out by reference to subsection 307-120(2) of the ITAA 1997. The proportion that the tax free component comprises of the superannuation interest is then calculated in accordance with section 307-125 of the ITAA 1997. This proportion is then applied to each benefit (ie, each payment) paid from the superannuation interest to determine the amount of the benefit that should be returned to the recipient as a tax free component. ***[Schedule 8, item 21]***

5.44 These changes to the ITAA 1997 require corresponding amendments to the social security definition of deductible amount. ***[Schedule 8, item 21]***

5.45 For defined benefit income streams created from 1 July 2007 (as well as those subject to an event under subsection 307-125(3) of the *Income Tax (Transitional Provisions) Act 1997)*, the rules under section 307-120 of the ITAA 1997 will also apply in

determining a deductible amount for social security purposes. Under these rules, the proportion of the superannuation interest that constitutes the tax free component will be applied to a benefit paid as an income stream payment to determine the tax free component, (ie, the deductible amount, for that benefit). ***[Schedule 8, item 21]***

5.46 For defined benefit income streams acquired before 1 July 2007, section 307-125 of the *Income Tax (Transitional Provisions) Act 1997* will apply in determining the deductible amount for social security purposes. The effect of this section is that the deductible amount for the income year will continue to be worked out under section 27H of the ITAA 1936 (as in force before 1 July 2007) unless a specific trigger event occurs under subsection 307-125(3). As the deductible amount calculated under section 27H is an annual amount, subsection 307-125(2) allocates the deductible amount proportionately to each of the income stream benefits paid out in respect of the year to which the deductible amount applies. If a trigger event occurs, the deductible amount will be assessed under the new rules in section 307-120 of the ITAA 1997. ***[Schedule 8, item 21]***

5.47 These methods of calculation will be applied irrespective of whether or not the recipient of the income stream payments is below 60 years of age, or 60 years of age or above. Where the recipients of defined benefit income streams are 60 years of age or above, it will still be necessary for them, or their provider, to retain details of the proportion of their superannuation interest that would have constituted the tax free component to allow the determination of their deductible amount for social security purposes. ***[Schedule 8, item 21]***

5.48 Deductible amounts for defined benefit income streams acquired before 1 July 2007 will not change for the life of the income stream unless a trigger event occurs. ***[Schedule 8, item 21]***

5.49 Deductible amounts for defined benefit income streams that are acquired from 1 July 2007, that are based on a proportion of the total superannuation interest, will remain constant for as long as the value of the benefits paid to the recipient remains constant. However, if the value of the benefits paid to the recipient rises, for example, as a consequence of indexation of the income stream payments, then the deductible amount will increase in line with an increase in the indexed payments. ***[Schedule 8, item 21]***

Schedule 9 — *Veterans' Entitlements Act 1986*

5.50 This Schedule amends the *Veterans' Entitlements Act 1986*.

Part 1 — Amendments commencing 20 September 2007

Removal of assets-test exemption for complying income streams and the retention of 100 per cent assets-test exemption for certain defined benefit income streams

5.51 Item 1 inserts new paragraph (aa) into subsection 5JA(1) of the *Veterans' Entitlements Act 1986*. Subsection 5JA(1) sets out the general requirements to be met for a lifetime income stream to be regarded as an assets-test exempt income stream. New paragraph (aa) provides that subject to new subsection 5JA(1AA), the relevant assets-test exempt income stream must have a commencement date that is prior to 20 September 2007. ***[Schedule 9, item 1]***

5.52 Item 2 inserts new subsection (1AA) into section 5JA. New subsection 5JA(1AA) provides that paragraph 5JA(1)(aa) is not applicable if the income stream is a defined benefit income stream. Income streams that are defined benefit income streams will be assets-test exempt regardless of the commencement date. ***[Schedule 9, item 2]***

5.53 Item 3 amends subsection 5JA(5) by omitting the words 'that does not meet the requirements of subsection (2)'. Subsection 5JA(5) provides the Repatriation Commission with the power to determine that an income stream was an assets-test exempt income stream even though it did not meet the requirements set out in subsection 5JA(2). The amendment to subsection 5JA(5) provides that the Repatriation Commission has the power to make a determination that any income stream is an assets-test exempt income stream whether or not the income stream's commencement date is before 20 September 2007. ***[Schedule 9, item 3]***

5.54 Item 4 inserts new subsections 5JA(5A) and (5B). New subsection 5JA(5A) provides that to avoid doubt, a determination of the Repatriation Commission under subsection 5JA(5) that an income stream is an assets-test exempt income stream can be made regardless of the commencement date of the income stream. New subsection 5JA(5B) provides that a determination of the Repatriation Commission under subsection 5JA(5) is not a

legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*. ***[Schedule 9, item 4]***

5.55 Item 5 repeals and substitutes subsection 5JB(1). Section 5JB sets out the general requirements to be met for a life expectancy income stream to be regarded as an assets-test exempt income stream. New paragraph 5JB(1)(a) provides that a life expectancy income stream will be regarded as an assets-test exempt income stream for the purposes of the *Veterans' Entitlements Act 1986* if the income stream has a commencement date before 20 September 2007 and subsection 5JB(1A) is applicable. ***[Schedule 9, item 5]***

5.56 Alternatively, new paragraph 5JB(1)(b) provides that the income stream will be an assets-test exempt income stream if subsection 5JB(1B) is applicable. Subsection 5JB(1B) is applicable in the circumstances where the Repatriation Commission has made a determination under subsection 5JB(4) that an income stream is an assets-test exempt income stream. ***[Schedule 9, item 5]***

5.57 Item 6 amends subsection 5JB(4) by omitting the words 'that does not meet the requirements of subsection (2)'. Subsection 5JB(4) provides the Repatriation Commission with the power to determine that an income stream is an assets-test exempt income stream even though it does not meet the requirements set out in subsection 5JB(2). The amendment to subsection 5JB(4) provides that the Repatriation Commission has the power to make a determination that any income stream is an assets-test exempt income stream whether or not the income stream's commencement date is before 20 September 2007. ***[Schedule 9, item 6]***

5.58 Item 7 inserts new subsections 5JB(4A) and (4B). New subsection 5JB(4A) provides that to avoid doubt, a determination of the Repatriation Commission under subsection 5JB(4) that an income stream is an assets-test exempt income stream can be made regardless of the commencement date of the income stream. New subsection 5JB(4B) provides that a determination of the Repatriation Commission under subsection 5JB(4) is not a legislative instrument. ***[Schedule 9, item 7]***

5.59 Item 8 amends subparagraph 5JBA(1)(a)(i) by omitting the words 'on or after 20 September 2004' and substituting the words 'during the period from 20 September 2004 to 19 September 2007 (both dates inclusive)'. Subsection 5JBA(1) sets out the general requirements to be met for a market-linked income stream to be

regarded as an assets-test exempt income stream. The amendment to subparagraph 5JBA(1)(a)(i) provides that the relevant assets-test exempt income stream must have a commencement day that is during the period from 20 September 2004 to 19 September 2007. ***[Schedule 9, item 8]***

5.60 Item 9 amends subsection 5JBA(11) by omitting the words 'that does not meet the requirements of subsection (2)'. Subsection 5JBA(11) provides the Repatriation Commission with the power to determine that an income stream is an assets-test exempt income stream even though it did not meet the requirements set out in subsection 5JBA(2). The amendment to subsection 5JBA(11) provides that the Repatriation Commission has the power to make a determination that any income stream is an assets-test exempt income stream whether or not the income stream's commencement date is before 20 September 2007. ***[Schedule 9, item 9]***

5.61 Item 10 inserts new subsections 5JBA(11A) and (11B). New subsection 5JB(11A) provides that to avoid doubt, a determination of the Repatriation Commission under subsection 5JBA(1) that an income stream is an assets-test exempt income stream can be made regardless of the commencement date of the income stream. New subsection 5JB(11B) provides that a determination of the Repatriation Commission under subsection 5JBA(11) is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*. ***[Schedule 9, item 10]***

Amendment to the definition of 'partially assets-test exempt income stream'

5.62 Item 11 repeals and substitutes the definition of 'partially assets-test exempt income stream' in subsection 52(1AA). Section 52 lists certain assets that are to be disregarded in the calculation of the value of a person's assets for the purposes of the means test applicable to payments of service pension or income support supplement. Included at paragraph 52(1)(daa) is a reference to 'half of the value of any partially assets-test exempt income stream'. ***[Schedule 9, item 11]***

5.63 The new definition provides that a partially assets-test exempt income stream is an income stream other than a defined benefit income stream as covered by subsection 5JA(1) or (1A) or 5JB(1) or 5JBA(1) and is an income stream that has a commencement date during the period from 20 September 2004 to

19 September 2007. For income streams commencing on or after 20 September 2007 only those income streams that are covered by principles determined by the Repatriation Commission in a legislative instrument will be regarded as being partially assets-test exempt. ***[Schedule 9, item 11]***

5.64 Item 12 repeals subsection 52(1AB) and inserts new subsections 52(1AB) and (1AC). New subsections 52(1AB) and (1AC) provide that the Repatriation Commission may determine principles for the purpose of determining whether or not an income stream is a partially assets-test exempt income stream. ***[Schedule 9, item 12]***

Reduction in assets-test taper rate

5.65 Item 13 amends paragraph 52Z(3)(d) by replacing a reference to '$19.50' with a reference to '$9.75' in the determination of the 'adjusted annual rate of ordinary income' for the purposes of the hardship provisions. That determination is made when the financial hardship rules are applicable to the determination of the rate of service pension or income support supplement. The amendment to paragraph 52Z(3)(d) reflects the change in the taper rate. ***[Schedule 9, item 13]***

5.66 Item 14 amends subpoint SCH6-F4(1) of Schedule 6 to the *Veterans' Entitlements Act 1986*. At the present time, the pension assets-test applies a taper rate that reduces a fortnightly service pension or income support supplement instalment by $3 for every $1,000 in assets above the relevant threshold. The taper rate is applied in the assets-test component of the Rate Calculators in Schedule 6 to the *Veterans' Entitlements Act 1986*. The reduction for assets in excess of the limit is calculated using the formula set out in point SCH6-F4. The proposed amendment will halve the taper rate to reduce instalments by $1.50 for every $1,000 in assets above the threshold. ***[Schedule 9, item 14]***

5.67 The determination of the amount of the excess assets is based on multiples of $250 and the current reduction is $0.75 per $250, being one quarter of the $3 per $1,000 reduction. The formula in subpoint SCH6-F4(1) currently includes a reference to '$19.50' as that figure was derived by *multiplying* 0.75 *by* 26. The excess of assets test is applied fortnightly so an annual figure is required for the Rate Calculator in determining an annual rate of service pension or income support supplement. This amendment will

replace the reference to '$19.50' with a reference to '$9.75'.
[Schedule 9, item 14]

5.68 Item 15 inserts a transitional provision that may be applicable in the circumstances where a claim for a service pension or income support supplement is made during the period from 20 September 2007 and 20 December 2007. ***[Schedule 9, item 15]***

5.69 Subclause 15(1) is applicable in the circumstances where a person is not receiving a service pension or income support supplement immediately before 20 September 2007 and subsequently makes a claim for a service pension or income support supplement during the 'claim period' which ends 20 December 2007. ***[Schedule 9, item 15]***

5.70 The effect of the provision is that service pension or income support supplement will only be payable from the later of 20 September 2007 or from the date of effect of the determination.
[Schedule 9, item 15]

5.71 Subclause 15(2) is also applicable in the circumstances where a person is not receiving a service pension or income support supplement immediately before 20 September 2007 and subsequently makes a claim for a service pension or income support supplement during the 'claim period'. ***[Schedule 9, item 15]***

5.72 The effect of the provision is that a person will be eligible for service pension or income support supplement in certain circumstances where service pension or income support supplement is not payable on the date of the claim. In those circumstances a service pension or an income support supplement will be payable if it would have been payable during a period that fell within the claim period and before the claim was made.
[Schedule 9, item 15]

Part 2 — Amendment commencing 1 July 2007

Amendment to the definition of 'deductible amount'

5.73 Item 16 repeals and substitutes the definition of 'deductible amount' in subsection 5J(1). The term 'deductible amount' is used in sections 46V and 46Y. Those sections concern the determination of the amount of income derived from the annual payments received from defined benefit income streams that are either assets-tested or assets-test exempt. ***[Schedule 9, item 16]***

5.74 This amendment to the definition of 'deductible amount' is a consequence of the amendments being made to the ITAA 1997 from 1 July 2007. The amended definition provides that for a defined benefit income stream the deductible amount is the sum of the amounts that are the tax free component of the payments received from the defined benefit income stream during the year. ***[Schedule 9, item 16]***

5.75 The tax free component of a payment will be determined under section 307-125 of the ITAA 1997 or if applicable, under section 307-125 of the *Income Tax (Transitional Provisions) Act 1997*. ***[Schedule 9, item 16]***

Chapter 6
Self-managed superannuation funds

Outline of chapter

6.1 Schedule 5 to this Bill amends the *Superannuation Industry (Supervision) Act 1993* and other Acts to enhance the regulation of self-managed superannuation funds and to ensure that self-managed superannuation funds comply with their legislative obligations.

6.2 Key changes include:

- streamlined reporting arrangements and the application of administrative penalties for late returns and false or misleading statements;
- clarification of trustee and auditor requirements; and
- other changes to the regulation of self-managed superannuation funds.

6.3 Schedule 5 to the Bill also amends the *Fringe Benefits Tax Assessment Act 1986* to remove fringe benefits tax (FBT) from *in specie* employer contributions to superannuation funds.

Context of amendments

6.4 Trustees of self-managed superannuation funds are required to comply with obligations under superannuation and taxation laws. These include lodging returns, complying with rules on member contributions and benefit payments, and complying with rules on superannuation investments. However, differing requirements under the various laws have resulted in inefficiencies and anomalies in relation to self-managed superannuation funds.

Reporting arrangements

6.5 Under current law, trustees of self-managed superannuation funds are required to lodge two separate returns or statements on different dates. They also pay the self-managed superannuation fund annual supervisory levy separately from their fund's income tax liability.

6.6 Administrative penalties for late returns and for making false or misleading statements do not apply to self-managed superannuation fund regulatory returns.

Trustee and auditor requirements

6.7 Trustee rules do not permit individual trustees of self-managed superannuation funds to receive remuneration for the performance of trustee duties or services. They also prevent a disqualified person from appointing a legal personal representative as a trustee of a self-managed superannuation fund. These trustee rules do not currently apply to directors of a corporate trustee of a self-managed superannuation fund.

6.8 Approved auditors are required to report actual and possible contraventions of the superannuation laws to the Regulator where the contraventions may affect the interests of fund members or beneficiaries. As a result, auditors may be uncertain about which matters should be reported to the Regulator.

Other regulatory changes

6.9 The regulatory provisions of the superannuation laws do not include relevant provisions of the taxation laws.

6.10 The Commissioner of Taxation (Commissioner), as Regulator of self-managed superannuation funds, cannot regulate funds which cease to be self-managed superannuation funds.

Fringe benefits tax

6.11 Employer contributions in cash to superannuation funds for the benefit of an employee are not subject to FBT. However, *in specie* contributions made by an employer are subject to FBT.

Summary of new law

6.12 The Government's superannuation reforms, *Simplified Superannuation*, announced on 5 September 2006 included specific proposals relating to the regulation of self-managed superannuation funds.

6.13 The number of self-managed superannuation funds has increased significantly over the past decade. Effective regulation of self-managed superannuation funds is crucial to the effective administration of *Simplified Superannuation* in the context of the growing number and size of such funds.

6.14 Improvements to the regulatory processes for self-managed superannuation funds will make their administration easier and simpler for trustees, reduce compliance costs and enhance self-managed superannuation fund compliance with both the current superannuation laws and the *Simplified Superannuation* reforms.

Reporting arrangements

6.15 Trustees of self-managed superannuation funds will lodge a single annual return and will make a single payment for both the supervisory levy and their fund's income tax liability.

6.16 Administrative penalties will apply to self-managed superannuation funds for failure to lodge documents on time and for making false or misleading statements on approved forms.

Trustee and auditor requirements

6.17 Trustee rules in respect of remuneration and legal personal representatives that apply to individual trustees will apply consistently to directors of a corporate trustee of a self-managed superannuation fund.

6.18 The reporting obligations of approved auditors will be clarified, so that auditors report on specified matters to the Regulator.

Other regulatory changes

6.19 The regulation of self-managed superannuation funds is improved by including provisions of the taxation laws, concerning both false or misleading statements and also superannuation fund reporting obligations, as regulatory provisions of the *Superannuation Industry (Supervision) Act 1993*.

6.20 The Commissioner will continue to regulate funds which have ceased to be self-managed superannuation funds until a person who holds a registrable superannuation entity licence is appointed as trustee of the fund.

Fringe benefits tax

6.21 FBT is being removed from *in specie* contributions to superannuation funds made by an employer for the benefit of its employees.

Comparison of key features of new law and current law

New law	*Current law*
Reporting arrangements	
Self-managed superannuation funds lodge a single annual return, and make a single payment for the fund's levy and income tax liability.	Self-managed superannuation funds lodge two returns or statements on different dates, and pay the levy separately from their income tax liability.
Administrative penalties for late returns and false or misleading statements will apply to self-managed superannuation funds.	Administrative penalties for late returns and false or misleading statements do not apply to self-managed superannuation fund regulatory returns.
Trustee and auditor requirements	
Directors of a corporate trustee cannot receive remuneration for trustee duties or be appointed a director in the capacity of a legal personal representative of a disqualified person.	Individual trustees cannot receive remuneration for trustee duties or be appointed as the legal personal representative of a disqualified person. These rules do not apply to directors of corporate trustees.
Approved auditors will report on	Approved auditors report

New law	*Current law*
matters specified in the approved form.	superannuation law contraventions that affect the interests of members or beneficiaries.
Other regulatory changes	
Provisions about false or misleading statements and superannuation fund reporting are included as regulatory provisions.	The regulatory provisions of the *Superannuation Industry (Supervision) Act 1993* do not include relevant taxation laws.
The Commissioner will continue to regulate former self-managed superannuation funds.	The Commissioner cannot regulate former self-managed superannuation funds.
Fringe benefits tax	
FBT is removed from *in specie* employer contributions to a superannuation fund.	*In specie* employer contributions to a superannuation fund are subject to FBT.

Detailed explanation of new law

Reporting arrangements

Definition of 'taxation law'

6.22 Amendments to the definition of 'taxation law' in the *Income Tax Assessment Act 1997* (ITAA 1997) and the *Taxation Administration Act 1953* (TAA 1953) facilitate the streamlined arrangements for self-managed superannuation funds, including:

- lodgement of a single annual return;
- collection and recovery of the supervisory levy; and
- application of administrative penalties to self-managed superannuation funds.

6.23 Prior to these amendments, the definition of 'taxation law' in the ITAA 1997 and the TAA 1953 referred to any Act of which the Commissioner has the general administration.

6.24 Most of the legislative obligations of self-managed superannuation funds are contained in the *Superannuation Industry (Supervision) Act 1993*, and the Commissioner has the general administration of the *Superannuation Industry (Supervision) Act 1993* to the extent it relates to self-managed superannuation funds (paragraphs 6(1)(e) and (f) of the *Superannuation Industry (Supervision) Act 1993*). It has long been considered that these specified provisions of the *Superannuation Industry (Supervision) Act 1993* are taxation laws for the purposes of the ITAA 1997 and the TAA 1953.

6.25 However, to avoid doubt, the definition of 'taxation law' in the ITAA 1997 is being amended to include a part of an Act to the extent to which the Commissioner has the general administration of that Act, and regulations under such a part of an Act. ***[Schedule 5, items 6 and 7, subsection 995-1(1) of the ITAA 1997]***

6.26 These amendments clarify that the previous definitions of taxation law in the ITAA 1997 and the TAA 1953 included the *Superannuation Industry (Supervision) Act 1993* to the extent that the Commissioner had general administration of that Act. To avoid the implication that there has been a substantive change in the meaning of taxation law, the amended definition is to be disregarded when interpreting the provision as it applied before the 2007-08 income year. ***[Schedule 5, item 8]***

6.27 The definition of 'taxation law' in the TAA 1953 is replaced by the amended definition in the ITAA 1997. This ensures that there is only one definition of 'taxation law'. ***[Schedule 5, item 31, subsection 2(1) of the TAA 1953]***

6.28 To avoid the implication that there has been a substantive change in the meaning of 'taxation law', the amended definition in the TAA 1953 is to be disregarded when interpreting the provision as it applied before the 2007-08 income year. ***[Schedule 5, item 32]***

6.29 A definition of 'self-managed superannuation fund' is also being inserted into the ITAA 1997 which refers to the definition of 'self-managed superannuation fund' in the *Superannuation Industry (Supervision) Act 1993*. ***[Schedule 10, item 66, subsection 995-1(1) of the ITAA 1997]***

Single annual return

6.30 Trustees of a self-managed superannuation fund are required to lodge a single annual return. The single annual return consists of the fund's income tax return, regulatory return, and a member contribution statement in respect of each member. This will result in a single lodgement date for the combined income tax return, regulatory return and member contribution statement.

6.31 The rationalisation of multiple reporting requirements is expected to reduce compliance costs for self-managed superannuation fund trustees, increase self-managed superannuation fund lodgement compliance, improve the quality of data provided to the Commissioner on the return and contribute to the effective administration of the contributions caps under the *Simplified Superannuation* reforms (see Chapter 7).

Supervisory levy

6.32 All superannuation funds, including self-managed superannuation funds, are subject to an annual supervisory levy designed to fund the regulatory costs of ensuring funds comply with their superannuation obligations. Administrative changes enable the payment of the supervisory levy to be incorporated into the payment of the fund's income tax liability.

6.33 The amended definition of 'taxation law' confirms that the collection and recovery provisions of the TAA 1953 apply to the supervisory levy, consistent with the processes for the self-managed superannuation fund's income tax liability.

6.34 The current penalty for the late payment of the supervisory levy is being repealed and replaced by the general interest charge (GIC). ***[Schedule 5, item 26, section 15DC of the Superannuation (Self Managed Superannuation Funds) Taxation Act 1987]***

6.35 The GIC provisions are contained in the TAA 1953. The supervisory levy is included in an index of provisions of Acts under which the GIC arises, other than provisions in the ITAA 1936. ***[Schedule 5, item 33, subsection 8AAB(5), item 13A in the table of the TAA 1953]***

6.36 The application of the GIC to the late payment of the supervisory levy is consistent with the treatment of the late

payment of the fund's income tax liabilities and is collected in the same way.

6.37 The reduction of multiple payment obligations eliminates the need for self-managed superannuation fund trustees to make two separate payments, while the streamlining of the late payment arrangements encourages timely payment of the supervisory levy. Both these initiatives are expected to result in simpler administration for trustees and reduced compliance costs.

6.38 As the late payment penalty for the supervisory levy is repealed, the following consequential amendments are required:

- The definition of 'late payment penalty' is repealed ***[Schedule 5, item 25, section 15DAA of the Superannuation (Self Managed Superannuation Funds) Taxation Act 1987].***
- The definition of 'general interest charge' is inserted ***[Schedule 5, item 24, section 15DAA of the Superannuation (Self Managed Superannuation Funds) Taxation Act 1987].***
- The reference to the late payment penalty is removed from the levy recovery provision ***[Schedule 5, item 27, section 15DD of the Superannuation (Self Managed Superannuation Funds) Taxation Act 1987].***
- References to the late payment penalty are removed from the levy payment provision ***[Schedule 5, items 28 and 29, section 15DE and Note of the Superannuation (Self Managed Superannuation Funds) Taxation Act 1987].***
- The reference to the late payment penalty is removed from the levy remission provision ***[Schedule 5, item 30, section 15DF of the Superannuation (Self Managed Superannuation Funds) Taxation Act 1987].***

6.39 These consequential amendments to remove references to the penalty for the late payment of the levy do not preclude the Commissioner's general recovery power under the TAA 1953.

Administrative penalties

6.40 Administrative penalties in the TAA 1953 for failing to meet certain obligations apply to trustees of self-managed superannuation funds. Administrative penalties enable the

Commissioner to take timely and effective action for breaches of a trustee's obligations.

Penalty for failing to lodge documents on time

6.41 An administrative penalty for failing to lodge documents on time applies to trustees of self-managed superannuation funds. The penalty will apply, for example, where the trustee of a self-managed superannuation fund fails to lodge the fund's single annual return on time. ***[Schedule 5, item 34, subsection 286-75(5) of the TAA 1953]***

6.42 Where the penalty is imposed on a corporate trustee, the directors of the body corporate at the time the body corporate becomes liable to the penalty are jointly and severally liable to pay the amount of the penalty. ***[Schedule 5, item 34, subsection 286-75(6) of the TAA 1953]***

6.43 The current penalty for the late lodgement of a self-managed superannuation fund's regulatory return is being repealed. ***[Superannuation (Self Managed Superannuation Funds) Supervisory Levy Amendment Bill 2006]***

6.44 The amendments extend the administrative penalty for the late lodgement of documents under taxation laws to self-managed superannuation funds and enable the Commissioner to collect the administrative penalty from the trustees or the directors of the corporate trustee. The amendments are expected to improve self-managed superannuation fund lodgement compliance.

Penalty for false or misleading statements

6.45 The current administrative penalty in the TAA 1953 for making false or misleading statements is imposed where the statement results in a tax shortfall. This penalty is not appropriate for self-managed superannuation funds, where false or misleading statements in relation to obligations under the *Superannuation Industry (Supervision) Act 1993* may not result in a tax shortfall.

6.46 An administrative penalty for false or misleading statements, including where the statements do not result in a tax shortfall, is being introduced for trustees of self-managed superannuation funds. ***[Schedule 5, item 35, section 288-85 of the TAA 1953]***

6.47 The penalty applies where the trustee makes a false or misleading statement in relation to the fund in an approved form given to the Commissioner or to another entity. The statement must be false or misleading in a significant way, either because of what is included in the statement or because of information omitted from the statement. ***[Schedule 5, item 35, subsection 288-85(2) of the TAA 1953]***

6.48 The penalty may be imposed on a trustee of a self-managed superannuation fund or on a trustee of a former self-managed superannuation fund which remains under the Commissioner's regulation (see paragraphs 6.69 to 6.76). ***[Schedule 5, item 35, subsection 288-85(1) of the TAA 1953]***

6.49 The maximum penalty is 20 penalty units. ***[Schedule 5, item 35, subsection 288-85(2) of the TAA 1953]***

6.50 Where a penalty is imposed on a corporate trustee, the directors of the body corporate at the time the body corporate becomes liable to the penalty are jointly and severally liable to pay the amount of the penalty. ***[Schedule 5, item 35, subsections 288-85(3) and (4) of the TAA 1953]***

6.51 The amendments enable the Commissioner to impose an administrative penalty on trustees of self-managed superannuation funds for making false or misleading statements on approved forms where the statements do not result in a tax shortfall. The penalty is expected to ensure the accuracy of information reported to the Commissioner and to other entities and to provide the Commissioner with greater flexibility in administering the law.

Trustee and auditor requirements

Trustee requirements

6.52 Directors of a corporate trustee cannot receive remuneration for the performance of trustee duties or services. This rule applies to directors of a corporate trustee of single member funds and of funds with more than one member. ***[Schedule 5, items 11 to 14, paragraphs 17A(1)(g) and (2)(d) of the Superannuation Industry (Supervision) Act 1993]***

6.53 A person, in the capacity of legal personal representative of a disqualified person, cannot be a director of a body corporate that is a trustee of a self-managed superannuation fund. ***[Schedule 5,***

item 15, subsection 17A(10) of the Superannuation Industry (Supervision) Act 1993]

6.54 These amendments extend the rules which apply to individual trustees to directors of a corporate trustee, ensuring consistent treatment in respect of trustee remuneration and legal personal representatives between individual trustees and directors of a corporate trustee.

6.55 The trustee rules relating to trustee remuneration and legal personal representatives form part of the basic conditions which a superannuation fund must satisfy in order to be a self-managed superannuation fund under section 17A of the *Superannuation Industry (Supervision) Act 1993*. A self-managed superannuation fund which breaches these rules may cease to be a self-managed superannuation fund (see paragraphs 6.69 to 6.76).

Auditor requirements

6.56 Approved auditors and actuaries of self-managed superannuation funds are required to report to the Regulator on matters specified in the approved form. ***[Schedule 5, item 22, paragraph 129(3)(c) of the Superannuation Industry (Supervision) Act 1993]***

6.57 This provision replaces the requirement under which approved auditors and actuaries of self-managed superannuation funds reported matters that may affect the interests of fund members or beneficiaries.

6.58 The approved form may refer to a class or classes of matters, rather than specific matters. ***[Schedule 5, item 23, subsection 129(3AA) of the Superannuation Industry (Supervision) Act 1993]***

6.59 An example of a class of matters would be matters relating to specific time periods. This would enable the Regulator to include in the approved form, for example, matters to be reported in relation to the fund's first year (or first full year) of operation. Targeting self-managed superannuation funds at, or very shortly after, their establishment would reduce the risk of non-compliance during the fund's future operations and allow the Regulator to take appropriate action at an earlier stage.

6.60 The matters able to be specified in the approved form are limited to contraventions of the *Superannuation Industry*

(Supervision) Act 1993 and its regulations and to matters relating to the annual audit of the fund's accounts.

6.61 These amendments apply only to self-managed superannuation funds and do not apply to approved auditors and actuaries of other regulated superannuation funds. ***[Schedule 5, item 20, paragraph 129(3)(b) of the Superannuation Industry (Supervision) Act 1993]***

Other regulatory changes

Regulatory provisions

6.62 The false or misleading statement provisions (see paragraphs 6.45 to 6.51) and the superannuation fund reporting requirements of the TAA 1953 are included (but only for self-managed superannuation funds) as regulatory provisions of the *Superannuation Industry (Supervision) Act 1993*. ***[Schedule 5, item 16, paragraph 38A(ab) of the Superannuation Industry (Supervision) Act 1993]***

6.63 A contravention of these provisions is a contravention of a regulatory provision regardless of whether it is an offence or a contravention of a civil penalty provision. ***[Schedule 5, item 18, paragraph 39(1)(c) of the Superannuation Industry (Supervision) Act 1993]***

6.64 A trustee of a self-managed superannuation fund is considered to contravene the false or misleading statement provisions by making false or misleading statements. ***[Schedule 5, item 19, subsection 39(1B) of the Superannuation Industry (Supervision) Act 1993]***

6.65 That is, conduct which may result in a penalty for false or misleading statements, regardless of whether the penalty is actually imposed by the Commissioner, is treated as a contravention of the false or misleading statement provisions of the TAA 1953.

6.66 The superannuation fund reporting requirements under *Simplified Superannuation* are explained in Chapter 7 of this explanatory memorandum. In relation to self-managed superannuation funds, trustees are required to lodge a member contribution statement in respect of each member. The member contribution statement will be included as part of the fund's single annual return. Trustees of self-managed superannuation funds may also be required to report to other entities, for example for roll-over purposes.

6.67 The Regulator may take appropriate action in response to a contravention of the regulatory provisions, including removing a fund's complying status under section 42A of the *Superannuation Industry (Supervision) Act 1993*.

6.68 The inclusion of the false or misleading statement provisions and the superannuation fund reporting requirements in the regulatory provisions supports the effective administration of the *Simplified Superannuation* reforms relating to member contributions and the contributions caps for self-managed superannuation funds.

Regulation of former self-managed superannuation funds

6.69 A superannuation fund is a self-managed superannuation fund if it satisfies certain conditions specified in section 17A of the *Superannuation Industry (Supervision) Act 1993*. Under current law, if the fund no longer satisfies any of these conditions, it ceases to be a self-managed superannuation fund six months after it failed to meet the condition, and is no longer regulated by the Commissioner (it ceases to be a self-managed superannuation fund immediately if the breach relates to the admission of a new member). The Australian Prudential Regulation Authority (APRA) becomes the regulator of the former self-managed superannuation fund.

6.70 A fund which has ceased being a self-managed superannuation fund will continue to be treated as a self-managed superannuation fund, for the purposes of sections 6, 42 and 42A of the *Superannuation Industry (Supervision) Act 1993.* The fund will continue to be treated as a self-managed superannuation fund for the purposes of these provisions until a person who holds a registrable superannuation entity licence is appointed as trustee. ***[Schedule 5, item 9, subsection 10(1) and item 10, subsection 10(4) of the Superannuation Industry (Supervision) Act 1993]***

6.71 The application of section 6 of the *Superannuation Industry (Supervision) Act 1993* to former self-managed superannuation funds enables the Commissioner to continue to regulate such funds, removing the need to change regulators to APRA and allowing the Commissioner to take timely and appropriate action where necessary.

6.72 The complying superannuation fund provisions (sections 42 and 42A of the *Superannuation Industry (Supervision) Act 1993*) determine whether a fund is a complying superannuation fund. Different compliance tests apply to self-managed superannuation funds and non-self-managed superannuation funds. In particular, the compliance test applying to self-managed superannuation funds requires all trustees to comply with the regulatory provisions. This test will now apply to all funds regulated by the Commissioner, including former self-managed superannuation funds.

6.73 A former self-managed superannuation fund will remain subject to all remaining provisions of the *Superannuation Industry (Supervision) Act 1993* that apply to regulated superannuation funds that are not self-managed superannuation funds.

6.74 A former self-managed superannuation fund remains under the Commissioner's regulation until a registrable superannuation entity licensee is appointed as trustee. At the time that a registrable superannuation entity licensee is appointed as trustee, APRA becomes the fund's regulator.

6.75 Alternatively, the trustees of the former self-managed superannuation fund may decide to wind up the fund.

6.76 If a registrable superannuation entity licensee is not appointed as trustee, and the fund is not wound up, the Commissioner, as Regulator, may take appropriate action. The Commissioner's actions could include suspending or removing a trustee and appointing an acting trustee, or removing a fund's complying status. The fund's complying status may be able to be removed because the trustees are in breach of the registrable superannuation entity provisions in the *Superannuation Industry (Supervision) Act 1993*.

Example 6.1

Demelza-Rose and John are members of their self-managed superannuation fund. Demelza-Rose resigns her position as a trustee of the fund, but remains a member.

The self-managed superannuation fund has breached one of the basic conditions of being a self-managed superannuation fund by having a member who is not a trustee.

The fund continues to be a self-managed superannuation fund until six months after Demelza-Rose ceased to be a trustee (subsection 17A(4) of the *Superannuation Industry (Supervision) Act 1993*). At the end of the six months, the fund will continue to be regulated by the Commissioner until the fund either appoints a registrable superannuation entity licensee as trustee or is wound up.

The fund may rectify the breach by Demelza-Rose becoming a trustee again, so that the fund again satisfies the conditions to be a self-managed superannuation fund. Alternatively, the fund may appoint a registrable superannuation entity licensee as trustee, in which case the Commissioner's regulation ceases.

If the fund takes no action, the Commissioner may take appropriate action, including:

- suspending or removing a trustee and appointing an acting trustee; or
- making the fund non-complying under section 42A of the *Superannuation Industry (Supervision) Act 1993*.

Fringe benefits tax

6.77 The definition of 'fringe benefit' in the *Fringe Benefits Tax Assessment Act 1986* in respect of a resident superannuation fund is amended to refer to 'contribution' rather than 'payment of money' or 'payment'. ***[Schedule 5, items 1 and 2, subparagraph 136(1)(j)(i) of the Fringe Benefits Tax Assessment Act 1986]***

6.78 The definition is also amended in respect of a non-resident superannuation fund. ***[Schedule 5, items 3 to 5, subparagraph 136(1)(j)(ii) of the Fringe Benefits Tax Assessment Act 1986]***

6.79 These amendments ensure that contributions made by an employer to a resident superannuation fund or to a non-resident superannuation fund for the benefit of an employee are specifically excluded from the definition of 'fringe benefit'. Consequently, such contributions are not subject to FBT.

6.80 A contribution may be either money or an *in specie* contribution, for example shares or real property.

6.81 The amendments provide consistent FBT treatment between employer contributions made in the form of money and *in specie* contributions made by employers.

6.82 Trustees of superannuation funds, and particularly self-managed superannuation funds, need to ensure that, in accepting *in specie* employer contributions, they do not contravene the investment rule that prohibits the intentional acquisition of an asset from a related party of the fund, including a member of the fund.

Application

6.83 The majority of the amendments apply to the 2007-08 income year, and later income years. For most self-managed superannuation funds, the 2007-08 income year commences on 1 July 2007, however, there may be some self-managed superannuation funds whose 2007-08 income year commences after 1 July 2007. ***[Schedule 5, item 36 and Superannuation (Self Managed Superannuation Funds) Supervisory Levy Amendment Bill 2006]***

6.84 The amendments providing an exemption from FBT for *in-specie* contributions to superannuation, the extension of the lodgement penalties to directors of corporate trustees, and the false and misleading statement provisions apply from 1 July 2007. ***[Schedule 5, item 36]***

Chapter 7
Other changes

Outline of chapter

7.1 Schedules 3, 4, 6 and 7 to this Bill contain administrative arrangements and the key elements of *Simplified Superannuation* not directly related to income tax. Broadly:

- Schedule 3 details the indexation provisions for certain thresholds applying to superannuation and employment termination payments.
- Schedule 4 streamlines superannuation fund reporting arrangements.
- Schedule 6 extends access to the Government co-contribution to the self-employed.
- Schedule 7 makes a minor amendment to the definition of 'unclaimed money' and provides for a consistent legislative basis in respect of portability requirements for superannuation funds and retirement savings account (RSA) providers.

Context of amendments

Indexation

7.2 A number of key superannuation tax thresholds are currently indexed annually to full-time average weekly ordinary time earnings, including reasonable benefit limits (RBLs), age-based limits and the eligible termination payment low-rate threshold. Indexation ensures that these thresholds maintain value over time relative to average full-time earnings.

7.3 *Simplified Superannuation* abolishes RBLs and age-based limits and introduces annual caps on superannuation

contributions. The new contribution thresholds will also be indexed to maintain value over time.

Superannuation fund reporting requirements

7.4 The existing legislative basis for the reporting of superannuation-related information to the Commissioner of Taxation (Commissioner) is fragmented and prescriptive. Superannuation entities provide information to the Commissioner, each other and individuals for co-contribution and superannuation guarantee (SG) purposes under separate legislation. Regulations detail the type of information to be provided. Additional reporting is required to support the new limits on superannuation contributions.

7.5 The penalties supporting the reporting requirements are similarly fragmented, resulting in anomalies in the severity and application of penalties for non-compliance. For example, under the *Superannuation (Government Co-contribution for Low Income Earners) Act 2003*, failure to provide a statement to another superannuation provider on transfers is a criminal offence (50 penalty units), whereas under the *Superannuation Guarantee (Administration) Act 1992* the same offence is classed as administrative (5 penalty units).

Co-contribution for the self-employed

7.6 The Government introduced the superannuation co-contribution scheme for low and middle income employees from 1 July 2003.

7.7 Currently, under the co-contribution scheme, the Government provides $1.50 for every $1 of personal superannuation contributions, up to the maximum co-contribution of $1,500. The maximum co-contribution is available to those individuals on incomes up to the lower threshold (currently $28,000) with the payment phasing out at the upper threshold (currently $58,000).

7.8 Self-employed individuals do not currently have access to the co-contribution unless 10 per cent or more of their income is attributable to eligible employment (ie, income earned as an employee).

Meaning of unclaimed money

7.9 Currently, an amount payable to a member of a fund is taken to be ***unclaimed money*** if:

- the member has reached the eligibility age specified in the regulations (currently 65);
- the superannuation provider determines that, under the governing rules of the fund or by operation of law, a benefit (other than a pension or annuity) is immediately payable in respect of the member;
- the superannuation provider has not received a contribution in respect of the member for at least two years; and
- after making reasonable efforts and after a reasonable period has passed, the superannuation provider is unable to ensure that the member receives the benefit.

7.10Prior to the removal of compulsory cashing on 10 May 2006, the effect of the definition in paragraph 7.9 was that the benefits of inactive members over the age of 65 who could not be contacted by their fund became unclaimed money. This arose because funds were required under law to cash the benefits of members over the age of 65 where they were unable to determine that the member satisfied the work test.

7.11 With the removal of compulsory cashing under *Simplified Superannuation*, the benefits of inactive members who have reached age 65 and who cannot be contacted by their fund are no longer immediately payable under law. The benefits of these members therefore do not become unclaimed money unless the rules of the particular fund require that a benefit is immediately payable to a member. The amendments change the definition of 'unclaimed money' to restore the previous effect of the law. This is achieved by removing the requirement for a benefit to be immediately payable in respect of a member.

Portability requirements

7.12 Since 1 July 2004, members of most superannuation funds have been able to move their superannuation benefits into a fund of their choice, subject to some limited exceptions (this is referred to as portability).

7.13 The legislative basis for the portability requirements of superannuation funds and RSA providers is inconsistent. In particular, the portability requirements for superannuation funds are specified in the *Superannuation Industry (Supervision) Regulations 1994*, whereas the requirements for RSA providers are specified in the *Retirement Savings Accounts Act 1997*. The penalties that apply for failure to comply with portability requirements are also inconsistent.

7.14 Under the *Superannuation Industry (Supervision) Act 1993*, complying with a portability request is an operating standard for the purposes of the Act and a breach of this standard attracts a penalty of up to 100 penalty units. If the portability requirements were similarly prescribed as a 'standard' for the purposes of the *Retirement Savings Accounts Act 1997*, the more detailed portability requirements could be contained in regulations and the penalty for failure to comply with a portability request could be made consistent with that which applies to superannuation funds.

Summary of new law

Indexation

7.15 Schedule 3 incorporates the indexation provisions for the new thresholds into the *Income Tax Assessment Act 1997* (ITAA 1997).

7.16 Existing indexation provisions (related to redundancy and early retirement scheme payments and pre-1 July 1988 funding credits) are also consolidated.

Superannuation fund reporting requirements

7.17 Schedule 4 creates a new Division in the *Taxation Administration Act 1953* (TAA 1953) which consolidates the existing

superannuation entity reporting requirements and new requirements under *Simplified Superannuation*.

7.18 The new Division contains the framework for approved reporting form contents, which allows the Commissioner to obtain the required information by designing approved forms in consultation with industry.

7.19 The uniform administrative and criminal penalty regime for non-compliance prescribed in the TAA 1953 applies.

Co-contribution for the self-employed

7.20 Schedule 6 extends the superannuation co-contribution scheme to the self-employed.

Meaning of unclaimed money

7.21 Schedule 7 amends the general meaning of unclaimed money in the *Superannuation (Unclaimed Money and Lost Members) Act 1999* to remove the requirement for a benefit to be immediately payable in respect of a member. Under the amendments, superannuation providers are required to make reasonable efforts to contact their inactive members over the age of 65 every five years to determine whether their benefits are unclaimed money.

Portability requirements

7.22 The portability requirements for RSA providers are removed from the *Retirement Savings Accounts Act 1997* and are inserted in the *Retirement Savings Accounts Regulations 1997*.

Comparison of key features of new law and current law

New law	*Current law*
Indexation	
Superannuation tax thresholds (except those relating to most transitional measures) are indexed annually to average weekly ordinary time earnings and rounded down to the nearest	Key superannuation tax thresholds are indexed annually to average weekly ordinary time earnings and rounded to the nearest dollar.

New law	Current law
multiple of $5,000.	
The indexation calculation utilises the original thresholds as of 1 July 2007 and the cumulative change in average weekly ordinary time earnings from the middle month of the December quarter 2006 to the middle month of the December quarter in the year preceding the year to which the new indexed threshold relates. The existing indexation arrangements using the March quarter figure is used for genuine redundancy payments and early retirement scheme payments and pre-1 July 1988 funding credits.	The indexation calculation is based on the previous year's thresholds and the annual change in average weekly ordinary time earnings up to the middle month of the March quarter preceding the year to which the new threshold relates.
Superannuation fund reporting requirements	
Superannuation entity reporting obligations in relation to contributions and benefits paid are consolidated.	Superannuation entity reporting obligations in relation to contributions and benefits paid are contained in separate legislation.
There are minimal details of approved reporting form contents in the legislation.	The content of reporting forms is prescribed in the legislation.
Penalties for non-compliance with reporting obligations are consolidated and standardised.	Penalties for non-compliance with reporting obligations are contained in separate legislation and are inconsistent.
Co-contribution for the self-employed	
The self-employed are eligible for the superannuation co-contribution.	The self-employed are not eligible for the superannuation co-contribution unless 10 per cent or more of their income is earned as an employee.
Meaning of unclaimed money	
The general meaning of unclaimed money is amended to remove the requirement for a	In order for an amount payable to a member to be unclaimed money, one of the conditions is

New law	Current law
benefit to be immediately payable in respect of a member. Superannuation providers are required to make reasonable efforts to contact their inactive members over the age of 65 every five years to ascertain the status of their benefits.	that a superannuation provider must determine that, under the governing rules of the fund or by operation of law, a benefit (other than a pension or annuity) is immediately payable in respect of a member. A further condition is that superannuation providers are required to make reasonable efforts to ensure that the member receives the benefit.
Portability requirements	
The portability requirements for RSA providers are specified in the *Retirement Savings Accounts Regulations 1997*.	The portability requirements for RSA providers are specified in the *Retirement Savings Accounts Act 1997*.

Detailed explanation of new law

Indexation

7.23 The thresholds that are subject to indexation and the corresponding areas of the tax law in which the thresholds can be found are listed in a table. Items 5 to 7 in the table consolidate existing indexation provisions (related to redundancy and early retirement scheme payments and pre-1 July 1988 funding credits), and items 8 to 12 are new items (related to superannuation and employment termination). The non-concessional cap is (and will remain) three times the concessional contributions cap. ***[Schedule 3, item 1, section 960-265]***

7.24 Thresholds related to transitional provisions are not indexed (with the exception of the transitional termination payment lower cap amount).

7.25 Existing indexation provisions related to genuine redundancy and early retirement scheme payments and pre-1 July 1988 funding credits are consolidated. While the wording is updated, it is not intended to change the meaning of these provisions. ***[Schedule 3, items 3, 5 and 6]***

7.26 The existing indexation provisions do not apply to items 8 to 12 in the table (related to superannuation and employment termination). ***[Schedule 3, items 2 and 4]***

7.27 New thresholds are indexed annually to average weekly ordinary time earnings and apply from 1 July each year. However, thresholds are rounded down to the nearest multiple of $5,000 to ensure thresholds remain in round figures. This should assist in maintaining simplicity and minimise the risk of inadvertent breaches of the excess contributions caps. ***[Schedule 3, item 7, subsections 960-285(1) and (2)]***

7.28 The indexation factor is the proportional change in average weekly ordinary time earnings from the middle month of the December quarter 2006 to the middle month of the December quarter just before the relevant income year. The indexation factor is calculated to four decimal places and rounded to three decimal places. ***[Schedule 3, item 7, subsections 960-285(4) to (6)]***

7.29 The amount cannot be reduced by indexation, that is, it is not indexed if the indexation factor is less than one. ***[Schedule 3, item 7, subsection 960-285(3)]***

Example 7.1

If the amount to be indexed is $50,000 and the indexation factor increases this to an indexed amount of $53,710 in the second year, the indexed amount is rounded back down to $50,000. In the third year, the new cumulative indexation factor is again applied to the $50,000 threshold and gives an indexed amount of $57,250. This amount is rounded down to $55,000.

If the $50,000 in this example represents the concessional contributions cap, the non-concessional contributions cap would be
$150,000 (3 × $50,000) in the first and second years and $165,000 (3 × $55,000) in the third year.

Once an individual breaches the non-concessional cap and activates the bring forward arrangements, the amount the individual can contribute over the three year period is based on the cap in the first year. Indexation of the cap in the second or third year does not increase the amount that can be brought forward. For example, if an individual makes a contribution of $450,000 in 2007-08, they are not able to make further contributions until 2010-11, even if the cap is increased during

that period. Similarly, if the individual first utilises the bring forward arrangements when the non-concessional contributions cap is $165,000, they are able to bring forward contributions of up to $495,000 over the three year period, even if indexation increases the amount of the non-concessional cap in the second or third years.

If the amount to be indexed is $1 million and the indexation factor increases this to an indexed amount of $1,043,000, the indexed amount is rounded back down to $1,040,000.

Superannuation fund reporting requirements

7.30 Several superannuation provider reporting obligations are rationalised in a new Division 390 of the TAA 1953.

Contributions statements

7.31 Superannuation providers are required to provide contribution statements to the Commissioner in the approved form in respect of individuals who were members at the end of the period, and also individuals who were members during the period and were paid superannuation benefits other than roll-over benefits. ***[Schedule 4, item 15, subsections 390-5(1), (3) and (4)]***

7.32 Where a superannuation provider rolls over a superannuation benefit, the paying provider does not have to provide a contribution statement to the Commissioner but is required to report to the receiving provider in respect of the amounts rolled over. The receiving provider is required to report the amounts in a contributions statement. ***[Schedule 4, item 15, section 390-5 and section 390-10]***

7.33 The approved form may require the statement to contain, among other things, details of contributions made or paid in respect of a member, including the amount and type of the contributions. ***[Schedule 4, item 15, subsection 390-5(9)]***

7.34 Contributions are taken to include notional taxed contributions and allocated surplus amounts. ***[Schedule 4, item 15, subsection 390-5(2)]***

7.35 Where the superannuation plan is a self-managed superannuation fund, the approved form may require the superannuation provider to supply a statement to the effect that no

contributions were made in respect of the member during the period. This assists the Commissioner to target his compliance activities for self-managed superannuation funds. ***[Schedule 4, item 15, subsections 390-5(1) and (9)]***

7.36 The approved form may also require the tax file numbers (TFNs) of the superannuation provider and the superannuation plan. In addition, if the member in respect of whom contributions are made has quoted their TFN to the superannuation provider, the approved form may also require the TFN of the member. This also applies if an individual making contributions on the member's behalf has legally provided the member's TFN to the superannuation provider. ***[Schedule 4, item 15, subsection 390-5(11)]***

7.37 The period covered by a statement and the day on which it must be provided are determined by the Commissioner. ***[Schedule 4, item 15, subsections 390-5(5) to (8)]***

7.38 The information collected by the Commissioner in the contribution statement may be used for co-contribution, SG and excess contributions cap purposes. Therefore, the approved form may contain any information the Commissioner may reasonably require to administer the legislation for those purposes. ***[Schedule 4, item 15, subsection 390-5(10)]***

Statements about superannuation benefits paid from one superannuation plan to another superannuation plan

7.39 Superannuation providers which transfer benefits on behalf of a member to another superannuation provider must supply the receiving provider with a statement in the approved form within seven days of making the transfer. The superannuation provider must also supply the affected member with a statement in the approved form within 30 days of making the transfer. ***[Schedule 4, item 15, sections 390-10 and 390-25]***

7.40 The approved form may require the statement to contain, among other things:

- details of the value of the superannuation benefit transferred, the tax free component, the taxable component, the element taxed in the fund and the element untaxed in the fund; and

- information about contributions made to the superannuation provider transferring the benefit in the financial year in which the transfer was made.

[Schedule 4, item 15, subsections 390-10(4) to (9)]

7.41 Contribution information is required to be reported to the other superannuation provider so it can provide an accurate contribution statement to the Commissioner for the relevant income year. ***[Schedule 4, item 15, sections 390-5 and 390-10]***

Superannuation statements to members

7.42 Arrangements for superannuation statements to members are maintained from the existing legislation. While the wording has been updated, it is not intended to change the meaning of the existing provisions. ***[Schedule 4, item 15, section 390-15]***

Statements relating to release authorities

7.43 Where a member or the Commissioner has requested via a release authority that a superannuation provider pay a liability using the member's superannuation monies and the superannuation provider has acted on that authority, the superannuation provider must supply the Commissioner with a statement in the approved form within 30 days of the amount being paid from the member's account. This reporting requirement exists even if the superannuation provider has paid the amount to the Australian Taxation Office (ATO) rather than to the individual. ***[Schedule 4, item 15, section 390-65]***

7.44 The approved form must include details of the release authority provided by the member or the Commissioner to the superannuation provider. ***[Schedule 4, item 15, subsection 390-65(4)]***

7.45 The approved form may require the statement to contain, among other things:

- details of the amount paid on behalf of or to the member;
- information about the superannuation provider; and
- information about the member who provided the release authority to the superannuation provider.

[Schedule 4, item 15, subsections 390-65(5) and (6)]

Change or omission in information given to the Commissioner

7.46 A superannuation provider must correct material errors or omissions in information supplied to the Commissioner within 30 days of becoming aware of them. The definition of 'material' depends on the particular facts and circumstances of each case. For example, if a member's contribution is initially reported as $1,000 where the amount is actually $2,000, that would generally be classed as a material change because of the relative difference between the two amounts. In contrast, an under-reporting by a few dollars would generally not be classed as a material change. A change may also be material because it does, or could, affect an individual's liability or entitlement. ***[Schedule 4, item 15, section 390-115]***

Example 7.2

ABC Superannuation Fund (ABC) is a large fund which reports contributions for the 2008-09 financial year for 20,000 members. Using the details contained in the report (after matching details from the member's tax return for the 2008-09 financial year), the ATO pays co-contributions and issues assessments of excess contributions taxes.

After checking with ABC in early 2009, Jonathon realises he has not been paid a co-contribution, even though he believes he satisfies the eligibility criteria (and has made personal contributions to ABC). He contacts the ATO which advises him that ABC did not report that he had made personal contributions for the 2008-09 financial year. Jonathon contacts ABC with details of the personal contributions he made during the 2008-09 financial year. ABC is required to correct this error and re-report the information to the ATO in respect of

Jonathon's account within 30 days of Jonathon contacting ABC and alerting it to the error.

In that same report, ABC mistakenly reports $100,000 of contributions for Nina instead of $10,000. The ATO issues Nina with an excess assessable contributions tax assessment because of this information. Nina contacts ABC and points out that the contribution made on her behalf was $10,000. ABC is required to re-report the information to the ATO in respect of Nina's account within 30 days of Nina contacting ABC and alerting it to the error.

Application

7.47 Superannuation fund reporting obligations, in relation to contributions, roll-overs and benefits paid, apply to things done or events occurring on or after 1 July 2007. These obligations will therefore apply where, for example, an amount is contributed to a fund or rolled over on or after that date, or where an individual holds a superannuation interest in a self-managed superannuation fund on or after that date. Reporting obligations for superannuation entities to provide statements about the release authorities (and to notify the Commissioner of material changes or omissions in relation to such statements) apply to release authorities given (and payments made in accordance with those authorities) on or after 10 May 2006. ***[Schedule 4, item 16 and Schedule 1, item 25, section 292-80 of the Income Tax (Transitional Provisions) Act 1997]***

Penalty regime

7.48 Penalties for non-compliance are standardised with the penalty regime under the TAA 1953. The existing TAA 1953 administrative and criminal penalties apply for late, or non-lodgement, of required statements and information. ***[Schedule 4, items 11 to 14]***

Co-contribution for the self-employed

Who is eligible for the co-contribution?

7.49 Individuals (including the self-employed) are eligible for the superannuation co-contribution if they meet certain criteria. First, they must earn 10 per cent or more of their total income from carrying on a business, eligible employment or a combination of both. Second, their total income (as reduced for individuals who

are entitled to deductions for carrying on a business) must be under the co-contribution upper income threshold. They must not be a temporary resident at any time during the income year in which the contribution is made, and be under age 71 at the end of that income year. ***[Schedule 6, items 1, 2, 7 and 8]***

Example 7.3

Susie is an Australian resident aged 26 who receives income from a religious vocation of $25,000 per year and also receives passive income of $2,000 per year. The definition of ***business*** within the meaning of the ITAA 1997 includes any profession, trade, employment, vocation or calling but does not include an occupation as an employee. Susie is carrying on a business for co-contribution purposes. As more than 10 per cent of her income is from carrying on a business, Susie would be eligible for a co-contribution payment if she makes personal contributions to her superannuation fund.

Example 7.4

Andrew is in a partnership and receives partnership income from carrying on a business of $45,000 per year. Andrew also receives $5,000 in passive income. Andrew's partnership income is business income for co-contribution purposes.

Which contributions qualify for a co-contribution payment?

7.50 The co-contribution is only available in respect of a personal superannuation contribution to the extent that the Commissioner has not allowed the contribution as a deduction. ***[Schedule 6, item 6, section 7]***

Example 7.5

Hector, a self-employed individual, makes a personal superannuation contribution of $5,000 to a complying fund on 30 June 2008. On 31 October, Hector claims a $4,000 deduction for this contribution in his 2007-08 income tax return, and his total income *less* business deductions is $28,000. The Commissioner receives contribution data from Hector's fund that $5,000 of personal contributions have been received. From the fund data and the income tax return, the Commissioner determines that $1,000 of the personal contribution is not deductible and that a co-contribution of $1,500 is payable into Hector's account.

7.51 To be a personal superannuation contribution that is eligible for co-contribution payment, the contribution must have been made on or after 1 July 2003 (by employees) or after 1 July 2007 (by the self-employed) to a complying fund or RSA to provide benefits for themselves, or to provide benefits on their death to their dependants. ***[Schedule 6, items 3 and 4, section 7]***

7.52 The following contributions are not eligible for a co-contribution: a roll-over superannuation benefit, a lump sum paid from a foreign superannuation fund, and a transfer from an overseas fund. ***[Schedule 6, item 5, section 7]***

How is total income for the year calculated?

7.53 Total income is used for determining the amount of co-contribution payable, and is the total of assessable income and reportable fringe benefits. Total income is reduced by amounts for which an individual is entitled to a deduction for carrying on a business. These deductions do not include work-related employee deductions or deductions that are available to eligible individuals (including the self-employed) for their personal superannuation contributions. The income concept used here is a *net* concept for individuals who carry on a business, and is designed to ensure that self-employed individuals with high gross business receipts are not arbitrarily exceeding the co-contribution income threshold. ***[Schedule 6, items 7 and 8]***

7.54 For the purposes of determining eligibility for the co-contribution, a total income concept is also used. However, in determining whether an individual satisfies the 10 per cent test (ie, 10 per cent or more of total income earned from eligible employment, carrying on a business or a combination of both), total income is not reduced by the deductions that result from carrying on a business. The income concept used here is a *gross* concept, designed to ensure that self-employed individuals with low incomes or low profit margins are not disadvantaged by arbitrarily failing the test. ***[Schedule 6, item 8, sections 6 and 8]***

Example 7.6

The use of the net and gross concepts of income mentioned above ensures that a self-employed individual with gross business receipts of $43,000, business deductions of $41,500, and other personal investment income of $15,000, would receive a

co-contribution because the percentage of gross income from employment or carrying on a business would be 74% ($43,000 / ($43,000 + $15,000))
and the net income for threshold purposes would be $16,500 ($43,000 + $15,000 – $41,500).

Meaning of unclaimed money

7.55 The requirement for a benefit to be immediately payable in respect of a member under the rules of the fund or by operation of law is removed from the definition of 'unclaimed money'. Superannuation providers are required to make reasonable efforts to contact their inactive members over the age of 65 every five years to determine whether their benefits are unclaimed money. ***[Schedule 7, items 2 to 6]***

7.56 The effect of the amendments is that the benefits of a superannuation fund member become unclaimed money once:

- the member has reached the eligibility age specified in the regulations (currently 65);
- the superannuation provider has not received a contribution on behalf of the member for at least two years; and
- after a period of five years since the superannuation provider last had contact with the member, the superannuation provider is unable to contact them again after making reasonable efforts.

Portability requirements

7.57 To ensure a consistent legislative framework for superannuation funds and RSA providers in respect of portability, the portability requirements for RSA providers are prescribed in the *Retirement Savings Accounts Regulations 1997*. To facilitate this, the specific provision in the *Retirement Savings Accounts Act 1997* covering portability is removed. ***[Schedule 7, item 1, section 50]***

Consequential amendments

Indexation

7.58 There are no consequential amendments.

Superannuation fund reporting requirements

7.59 Several consequential amendments are required to remove current reporting requirements that are being consolidated as part of the new law. ***[Schedule 4, items 1 to 10]***

Co-contribution for the self-employed

7.60 There are no consequential amendments.

Meaning of unclaimed money

7.61 There are no consequential amendments.

Portability requirements

7.62 There are no consequential amendments.

Chapter 8
Regulation impact statement

Policy objective

8.1 The policy objective is to simplify superannuation for retirees making it easier to understand, improve incentives to work and save, and introduce greater flexibility in how superannuation savings can be drawn down in retirement.

Background

8.2 The Government is committed to Australia's three-pillar approach to providing retirement incomes, which has been broadly endorsed by the World Bank. The three pillars comprise:

- a taxpayer funded means-tested age pension for people who are unable to fully support themselves in retirement;
- a minimum level of compulsory employer superannuation contributions made in respect of employees; and
- voluntary private superannuation and other savings.

8.3 This three-tiered approach efficiently and effectively achieves the multiple functions of retirement income policy, which include poverty alleviation and wealth redistribution, increasing private savings, improving retirement incomes and managing risk, while promoting workforce participation. Australia's retirement income system complements Government policies designed to encourage labour force participation, maximise productivity and ensure long-term fiscal sustainability.

8.4 Australia's superannuation system comprises the second and third pillars. Its objective is to assist and encourage people to achieve a higher standard of living in retirement than would be

possible from the age pension alone, to ensure Australians have security and dignity in retirement.

8.5 In pursuit of this objective, the Government provides significant superannuation taxation concessions, valued at $15.9 billion in 2005-06. The Government also provides targeted assistance through initiatives such as the superannuation co contribution for low to middle income employees, capital gains tax exemptions for small business owners and the Mature Age Worker Tax Offset for older workers.

8.6 However, there is growing recognition that the efficiency and effectiveness of Australia's superannuation system is being impeded by unnecessarily complex and prescriptive rules.

8.7 In the 2006-07 Budget, the Government announced a plan to simplify and streamline superannuation. A detailed document outlining the Government's proposals, *A Plan to Simplify and Streamline Superannuation*, was released on Budget night, 9 May 2006.

8.8 Key stakeholders and members of the community were invited to make comments and submissions on the plan during the three-month consultation period. After considering the outcomes of consultation, the Government announced its final policy decision, *Simplified Superannuation*, on 5 September 2006.

8.9 The package of reforms detailed in *Simplified Superannuation* will sweep away the current raft of complex tax arrangements and restrictions that apply to people's superannuation benefits. Simplification will increase community understanding and, when combined with more flexibility and greater tax concessions, will encourage individuals to take greater interest in their superannuation. The Government's reforms will also provide individuals with clear incentives to save and to work longer.

Impact groups

8.10 *Simplified Superannuation* is expected to impact on the following groups:

- individuals (including the self-employed);
- employers;
- superannuation funds (including approved deposit fund and retirement savings account (RSA) providers, and self-managed superannuation funds); and
- the Government.

Specific issues

8.11 This part of the Chapter will identify the objectives of the Government's reforms. It will explore options to ameliorate existing systemic problems, assessing the costs and benefits of each option for the impact groups identified in paragraph 8.10. The optimal approach for addressing each objective will then be identified.

8.12 The options in this section largely reflect the reforms outlined in *Simplified Superannuation*. However, where consideration was given to an alternative approach for satisfying a particular objective, the alternative is separately assessed. Linkages between each option are identified and discussed.

8.13 Paragraphs 8.14 to 8.166 contain qualitative assessments of the costs and benefits of the key policy proposals in *Simplified Superannuation*. Quantitative assessment is in paragraphs 8.167 to 8.171.

Simplification of the taxation arrangements for superannuation by reducing the number of taxing points

Problem identification

8.14 The superannuation system has a myriad of different arrangements for tax on contributions, earnings and benefits.

8.15 In relation to the average person, employer and concessional member superannuation contributions are taxed at the concessional rate of 15 per cent. Personal contributions made

from after-tax income for which no deduction has been claimed are not subject to further tax in the superannuation fund.

8.16 The investment income of superannuation funds is taxed at 15 per cent, but can be reduced through the use of imputation credits.

8.17 The tax treatment of superannuation benefits depends on a range of factors, including whether the individual:

- commenced work before 1 July 1983;
- already received some of their superannuation benefits or contributed an employment termination payment;
- chose to withdraw their benefits as a lump sum or as a pension;
- claimed a deduction; and
- the type of pension product purchased, if the recipient elected to receive their benefits as a pension.

8.18 The complexity of the superannuation taxation arrangements impacts on all retirees, irrespective of the amount of money they have accumulated in superannuation. This complexity confuses retirement decisions, clouds the incentive to invest in superannuation and imposes unnecessary costs.

8.19 The transition to retirement is a significant time in a person's life and the superannuation taxation arrangements unnecessarily complicate this transition. People must pay for professional advice or spend hours of time trying to understand the tax treatment of their superannuation.

8.20 Individuals who receive their benefits may not know if they have exceeded their reasonable benefit limit (RBL) (and hence will be required to pay additional tax) until they have lodged their tax return for the period in which the benefits were received.

8.21 The Peter Hendy and Dick Warburton authored report, *International Comparison of Australia's Taxes*, noted that Australia is one of the only countries in the world to tax superannuation at three points. It suggested that the taxation of both contributions

and benefits serves to exacerbate system complexity and imposes high compliance costs.

8.22 The report of the Taskforce on Reducing Regulatory Burdens on Business, *Rethinking Regulation*, described Australia's superannuation system as highly complex and recommended that high priority be given to comprehensive simplification of the tax rules for superannuation benefits.

Options

Option One: Removal of the tax levied on superannuation benefits paid from a taxed source to individuals aged 60 years and above

8.23 All lump sum and pension payments (including pensions which commenced before 1 July 2007) would be tax free when paid to individuals aged 60 and over from a taxed source (where contributions and earnings tax has been paid). Additional concessions would be introduced for benefits paid from untaxed sources (where contributions and earnings tax has not been paid, primarily affecting public servants and members of the military), to ensure a similar tax treatment between benefits paid from taxed and untaxed sources. RBLs would be abolished for all individuals.

8.24 As the tax treatment of employment termination payments is based on RBLs, the employment termination rules would also be modified.

Benefits

Individuals (including the self-employed)

8.25 The elimination of benefits tax would have a significant impact on an individual's retirement income. An average income earner whose sole contribution to superannuation comprises superannuation guarantee (SG) payments over a working life of 40 years would have an additional lump sum of around $37,000 in retirement or an additional $136 per week if they took their benefit as a superannuation pension.

8.26 Individuals aged over 60 receiving lump sum or pension payments from a taxed source would not need to include details of these payments in their tax returns, lowering their taxable income and therefore potentially lowering the tax paid on other income.

This would increase the incentive for individuals to undertake work while drawing down on superannuation.

8.27 The report of the Taskforce on Reducing Regulatory Burdens on Business, *Rethinking Regulation*, highlighted that the greatest area of complexity in the current superannuation system is the taxation of end benefits. For example, under the current system, a lump sum may include up to eight different parts taxed in seven different ways.

8.28 Option One would yield significant simplicity benefits for retirees. The thousands of Australians who turn 60 each year and choose to retire would have a much simpler system to face when deciding how to draw on their superannuation. They would no longer need to pay for expensive financial advice on the tax treatment of their superannuation benefits. Independent evidence given to the House Standing Committee on Economics, Finance and Public Administration inquiry into improving the superannuation savings of people under age 40 stated that this advice can currently cost in the order of $3,000 to $10,000 depending on the complexity.

8.29 The reduction in complexity could also be expected to decrease the costs facing superannuation schemes in delivering their services over the longer term, potentially benefiting individuals through a reduction in fees and charges. The impact of the reduction in complexity for superannuation funds is explored in paragraphs 8.32 to 8.34.

8.30 The February 2006 update of the Australian Bureau of Statistics' *Retirement and Retirement Intentions Survey* indicated that 19 per cent of people in the labour force intend to retire between the ages of 55 and 59. The continued application of benefits tax for individuals aged under 60 who receive payments from both taxed and untaxed sources would provide an incentive for these individuals to remain in the workforce and leave their superannuation benefits in their funds until they turn age 60. If an individual chooses to work and contributes to superannuation in this time, their retirement savings would be further boosted through additional contributions and earnings.

Employers

8.31 Employers would benefit from a reduction in the number of forms required to process an employment termination payment entitlement.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.32 The removal of benefits tax would reduce the myriad of rules and red tape that superannuation funds must contend with when paying out a benefit. Funds would no longer need to report benefit payments paid to members and commutations of pensions for RBL purposes. As most superannuation pensions would be tax free, funds would no longer be required to withhold tax instalments from these benefits and provide recipients with a payment summary. The requirement to withhold tax from lump sum payments paid to a person aged 60 or over would be removed, and funds would no longer be required to provide payment summaries to these taxpayers.

8.33 Funds would also benefit through the reduction in the number of benefit components on which records must be maintained (reduced from eight to two).

8.34 The reduction in complexity achieved through the removal of end benefits tax could also be expected to decrease the costs facing superannuation schemes in delivering their services.

Government

8.35 The Australian Taxation Office (ATO) would experience a reduction in the number of taxpayers who are required to lodge tax returns each year (around 152,000 taxpayers per annum based on 2004-05 tax return data) as a result of the abolition of end benefits tax.

8.36 The ATO would also experience an associated reduction in income tax return processing and potentially debt collection cases due to a reduction in the number of clients in the income tax system.

Costs

Individuals (including the self-employed)

8.37 The proposed removal of end benefits taxation would require revisions to the existing superannuation contribution rules to ensure appropriate limits on the level of tax concessions provided to individuals. These revisions and their impacts are discussed in paragraphs 8.55 to 8.74.

8.38 Individuals may need to seek clarification and advice on the new arrangements from financial planners and superannuation funds.

Employers

8.39 Employers who pay employment termination payments would need to update their systems and processes to reflect the new employment termination arrangements.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.40 Superannuation funds may incur short-term costs associated with the need to review and adapt existing record-keeping systems and processes (both electronic and manual); however, these costs would be recovered from fund members over the longer term.

8.41 In addition, superannuation funds would incur implementation costs associated with training staff, updating

product disclosure statements, and communicating the changes to members.

Government

8.42 The ATO may require additional resourcing to update its technical and information products (electronic and printed) to advise its clients of the proposed changes.

Option Two: Removal of the tax on superannuation contributions

8.43 The 15 per cent tax levied on superannuation contributions would be abolished for all individuals.

8.44 Option Two would also necessitate changes to end benefits taxation to reflect that some benefits have been subject to the tax on contributions while others have not.

Benefits

Individuals (including the self-employed)

8.45 The elimination of the tax on contributions would impact on an individual's retirement income. An average income earner whose sole contribution to superannuation comprises SG payments over a working life of 40 years would have an additional $17 per week if they took their benefit as a superannuation pension.

8.46 Option Two may increase the incentive for individuals to make additional salary sacrifice contributions, further improving retirement incomes. It may also increase the incentive to work, by decreasing the effective tax paid by individuals on their labour income. However, increases in retirement income generated by the removal of the tax on contributions would be clawed back to some degree by the pension assets test.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.47 The abolition of the tax on contributions would benefit superannuation funds by increasing the level of funds available for investment, potentially generating higher earnings. Superannuation funds may also receive some cost savings by no longer having to withhold tax on contributions.

Other

8.48 Employers and the Government would not receive additional benefits.

Costs

Individuals (including the self-employed)

8.49 Option Two may further complicate the taxation of benefits. It would require both the apportioning of the amount of benefits on which tax was paid and a new lump sum component to be added for benefits accumulated from the removal of the tax on contributions. This component would then be taxed at an additional 15 per cent to what currently applies.

8.50 In addition, the 15 per cent superannuation pension rebate introduced in 1988 to compensate individuals for the imposition of the tax on contributions would need to be abolished for any part of a pension accumulated after the removal of the tax on contributions.

8.51 Individuals would continue to include superannuation lump sum or pension payments in their assessable income, maintaining the disincentive to work while drawing down on superannuation.

Other

8.52 Employers, superannuation funds and the Government would not incur additional costs.

Recommendation

8.53 It is recommended that Option One be adopted.

8.54 Option One is considered preferable to Option Two, as the benefits expected from Option One are greater than those for Option Two and the associated costs would be less.

- A key objective of the Government's reforms is to reduce the complexity imposed on retirees. The complexities of the current system would remain if the tax on superannuation contributions was reduced or even removed.

- The abolition of end benefits taxation, coupled with the reduction in the age pension assets-test taper rate envisaged in paragraphs 8.94 to 8.104, will result, on average, in higher retirement incomes than the removal of the tax on contributions at a lower cost. Option One will also provide individuals with greater incentives to remain in the workforce until at least age 60.
- The ongoing compliance savings for both individuals and superannuation funds from the abolition of end benefits tax and RBLs are substantially larger than the initial implementation costs.
- Removing the tax on contributions:
  - would not have the same benefits on participation as the removal of end benefits tax as the draw down of superannuation would be included in the assessable income of the taxpayer, potentially increasing the tax on their work income; and
  - would result in a significantly higher cost to revenue.

Simplification of contribution rules

Problem identification

8.55 Currently, individuals must contend with complex and prescriptive rules when deciding to contribute to superannuation. Employers are able to claim a full deduction for contributions made on behalf of an employee up to the employee's age-based limit; in 2006-07 the aged-based limits are:

- $15,260 for individuals aged under 35 years;
- $42,385 for individuals aged 35 to 49; and
- $105,113 for individuals aged 49 to 69.

Employers are denied a deduction for contributions above the relevant limit. The age-based limits are a source of complexity in the superannuation system.

8.56 The proposed abolition of RBLs and end benefits taxation would create an incentive for high-wealth individuals to transfer large amounts of assets currently held outside of superannuation to the concessionally taxed superannuation system. The existing contribution rules would therefore need to be streamlined and tightened to ensure appropriate limits are applied on the level of tax concessions provided to individuals.

Options

Streamlined rules for concessional contributions

8.57 Age-based limits would be removed and a uniform limit on concessional contributions of $50,000 per person per annum would apply. These contributions would be taxed at 15 per cent. The proposed limit has been set with reference to the current median age-based limit.

8.58 Where the ATO identifies that a person's concessional contributions have exceeded $50,000 in a financial year, the amount in excess of $50,000 would be taxed at the top marginal rate (plus the Medicare levy). Excess concessional contributions would be included in the cap on non-concessional contributions (see paragraphs 8.61 to 8.63).

8.59 In cases where a tax file number (TFN) has not been quoted, the top marginal rate (plus the Medicare levy) would be withheld from concessional contributions over $1,000. The $1,000 threshold would not apply to new accounts.

8.60 Employers would be able to claim a full deduction for all contributions to superannuation funds made on behalf of their employees under age 75.

New rules for post-tax (non-concessional) contributions

8.61 A cap of $150,000 per year on the amount of non-concessional superannuation contributions a person can make would apply. Eligible individuals under age 65 would be able to bring forward two years of contributions to accommodate larger one-off payments.

8.62 Where the ATO identifies that a person has breached the cap, excess contributions would be taxed at the top marginal rate plus the Medicare levy.

8.63 Superannuation funds would only be able to accept non-concessional contributions for or on behalf of a member if the member's TFN has been quoted to the trustee.

Impact analysis

Benefits

Individuals (including the self-employed)

8.64 The proposed removal of age-based limits would provide scope for employees under age 35 to make larger contributions to superannuation through salary sacrifice arrangements, as their employers would be able to claim a full tax deduction for all contributions. The current age-based limit for individuals less than age 35 is $15,260 per annum, compared to the proposed limit of $50,000 per annum.

Employers

8.65 Employers would benefit from their ability to claim a full deduction for superannuation contributions made on behalf of employees up to age 75. They would no longer be required to monitor the level of superannuation contributions against age-based limits to determine if they can claim a deduction.

Other

8.66 Superannuation funds and the Government would not receive additional benefits.

Costs

Individuals (including the self-employed)

8.67 The proposed cap on non-concessional contributions may impact unfavourably on a small number of individuals who wish to transfer amounts greater than $450,000 (allowing for the two year bring forward arrangements) into superannuation.

8.68 The cap on non-concessional contributions is expected to impact on relatively few individuals.

8.69 It is estimated that currently less than one per cent of people aged 65 and below who make non-concessional contributions to superannuation would contribute more than $450,000 in a year. The impact of the cap on these individuals would be mitigated through a number of exemptions and transitional arrangements.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.70 While additional tax payable for excess concessional contributions would be levied on individual members, superannuation funds may be required to arrange for the payment of the additional tax if requested by a member.

8.71 In addition, superannuation funds would be required to withhold tax on concessional contributions where a member's TFN has not been reported, and refund tax withheld if the TFN is subsequently reported.

Government

8.72 The ATO would require additional resourcing to manage the increased administrative workflow resulting from the need to monitor the level of individuals' concessional and non-concessional contributions and assess tax on excess contributions.

Other

8.73 Employers would not incur additional costs.

Recommendation

8.74 It is recommended that the proposed streamlined rules for concessional contributions and non-concessional contributions be adopted. The new rules will allow individuals to contribute more concessionally taxed money into superannuation from a younger age and will be significantly easier to understand. While the new rules may impact unfavourably on a very small number of individuals and will involve implementation and ongoing costs for superannuation funds, they will be mitigated through a number of

exemptions and transitional arrangements and will play a key role in the fiscal sustainability of the Government's reform package.

Simplification of payment rules

Problem identification

8.75 The Government recognises that for the superannuation system to be efficient, superannuation rules and regulations must be understandable, send clear signals and provide appropriate incentives. Impediments, complexity and rigidity should be minimised.

8.76 The existing rules regulating matters such as how benefits are to be taken, coupled with the forced payment of benefits once an individual reaches age 65 and no longer satisfies the work test (ie, has not worked at least 40 hours during a consecutive 30 day period in a financial year), are complex and limit individual choice.

8.77 These rules discourage market innovation, and result in decisions being driven by product tax / social security treatment. In addition, they impose unnecessary costs on superannuation funds which have to administer a work test for all members aged 65 to 74 who have not yet taken their benefits, to determine whether the benefits of these members must be paid.

Options

Abolition of compulsory withdrawal

8.78 The requirement for compulsory payment of benefits to members over age 65 who do not meet the current work test would be removed — that is, there would be no forced payment of superannuation benefits after age 65. The requirement that benefits must be paid out regardless of a person's work status from age 75 would also be removed.

Streamlined pension rules

8.79 All pensions that meet simplified minimum standards would be taxed the same on payment.

8.80 The new minimum standards for pensions commencing on or after 1 July 2007 would require:

- payments of a minimum amount to be made at least annually, allowing pensioners to take out as much as they wish above the minimum (including cashing out the whole amount);
- no provision to be made for an amount to be left over when the pension ceases; and
- that the pension could be transferred only on the death of the pensioner to one of their dependants or cashed as a lump sum to the pensioner's estate.

8.81 The payment rules would specify minimum limits only. No maximum would apply, with the exception of pensions which are commenced under the transition to retirement condition of release.

8.82 Pensions which commenced prior to 1 July 2007, which complied with relevant rules for the transition to retirement measure at the time, would be deemed to satisfy the proposed requirements.

Impact analysis

Benefits

Individuals (including the self-employed)

8.83 Individuals would benefit from greater flexibility, as they would no longer be forced to draw down on their superannuation benefits after age 65. Subject to fund rules, superannuation could be paid out whenever and however an individual wished. Individuals could withdraw as much or as little as they wanted from superannuation and it would generally not need to be included in their tax return. Moreover, individuals would have the freedom to change their arrangements as their circumstances change.

8.84 Lower drawdowns in the earlier years of a pension would result in greater capital accumulation and longer pension terms. The changes to the pension drawdown rules would also improve

the likelihood that pensions will easily adapt to improvements in life expectancy. This would provide increased certainty that individuals would not outlive their retirement savings.

8.85 Individuals may also benefit from greater product choice and lower fees and charges brought on by the deregulation of the pension product market.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.86 Superannuation funds would no longer have to administer work tests to determine whether the benefits of members aged between 65 and 74 must be paid out.

8.87 The deregulation of the pension product market would benefit superannuation funds by providing them with greater scope for innovation.

Other

8.88 Employers and the Government would not receive additional benefits.

Costs

Individuals

8.89 Members may need to seek clarification and advice on the new streamlined rules from their superannuation funds.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.90 Superannuation funds may need to seek advice about changing their investment strategies due to possibly changed cash flow requirements applicable to the new products they would be able to market in accordance with the new pension rules. They may also need to seek advice as to whether their trust deeds should be updated to reflect the new streamlined rules.

8.91 In addition, superannuation funds may also need to manage enquiries from their members who are seeking clarification and advice concerning the new streamlined rules.

Other

8.92 Employers and the Government would not incur additional costs.

Recommendation

8.93 It is recommended that the abolition of compulsory withdrawal and the introduction of streamlined pension rules be adopted. The abolition of compulsory withdrawal will provide individuals with greater freedom and flexibility. The new pension rules will benefit individuals through greater product choice and lower fees and charges. While individuals will face initial implementation costs, they will receive substantial ongoing compliance savings through these amendments. Similarly, while superannuation funds may incur initial implementation costs from the need to change investment strategies, update trust deeds and advise members of the proposed changes, these costs will be offset by substantial ongoing compliance savings.

Reduction in the pension assets-test taper rate

Problem identification

8.94 The existing pension assets-test taper rate is very punitive as retirees must achieve a return of at least 7.8 per cent on their additional savings to overcome the effect of a reduction in their age pension amount.

8.95 The current assets test also prevents existing retirees with relatively modest assets but with low incomes from being able to access the age pension. Under the current system, a single homeowner would lose part of their pension once their assets exceed $161,500.

8.96 The introduction of more generous pension assets-test rules would greatly increase incentives to save.

Options

Halving the pension assets-test taper rate

8.97 The pension assets-test taper rate would be halved from 20 September 2007 so that recipients only lose $1.50 per fortnight

(rather than $3) for every $1,000 of assets above the relevant threshold.

Abolishment of the assets-test exemption for complying income streams

8.98 The 50 per cent assets-test exemption for complying income streams would also be abolished from 20 September 2007, with all new pensions receiving uniform age pension treatment. Retaining the assets-test exemption would enable high wealth individuals to access the age pension.

Impact analysis

Benefits

Individuals (including the self-employed)

8.99 The proposal to halve the assets-test taper rate would mean that retirees would need to achieve a return of 3.9 per cent on their additional savings before they are better off in net income terms — that is, after taking into account the withdrawal of the age pension. Based on the current age pension, the proposal would enable a single retiree homeowner to have around an additional $172,000 of assets before losing the age pension, while a couple could have approximately $287,000 of additional assets. The proposal would therefore generate significant incentives for individuals to work and save.

Other

8.100 Employers, superannuation funds and the Government would not receive additional benefits.

Costs

Individuals (including the self-employed)

8.101 From 20 September 2007, an assets-test exemption would no longer apply for certain income streams. However, the effects of the removal of the exemption are expected to be offset for most individuals through the reduction in the assets-test taper rate.

8.102 The abolition of the assets-test exemption is required to limit the scope for wealthier individuals to access the age pension.

If the assets-test exemption was maintained, the age pension could potentially be extended to high wealth individuals, undermining the spirit of the age pension arrangements.

Other

8.103 Employers, superannuation funds and the Government would not incur additional costs.

Recommendation

8.104 It is recommended that the reduction in the assets-test taper rate be adopted. The reduction will encourage and reward individuals to work and make additional savings, supporting the Government's objective of encouraging self-provision in retirement.

Improved incentives for superannuation contributions by the self-employed

Problem identification

8.105 Under the current system, the self-employed may have less incentive to contribute to superannuation than employees.

8.106 Under the current system, employers are able to claim a full deduction for contributions made on behalf of employees up to the relevant age-based limit. In addition, low and middle income employees are eligible for the Government's co-contribution scheme (which matches $1.50 for every $1 of post-tax superannuation contributions made by low and middle income employees, up to a maximum of $1,500 for employees earning below $28,000 and phasing out completely for employees earning over $58,000).

8.107 In contrast, self-employed persons are only entitled to claim a full deduction for the first $5,000 contributed to a complying superannuation fund in a financial year. Contributions above this amount are 75 per cent tax deductible, up to a maximum deduction equal to the relevant age-based limit. Moreover, self-employed persons are not eligible for the Government's co-contribution scheme.

8.108 The current contribution arrangements for the self-employed may discourage the self-employed from making larger contributions to superannuation.

Options

Removal of the 75 per cent limit on deductions for superannuation contributions over $5,000 made by the self-employed

8.109 The deductibility of superannuation contributions by the self-employed (and other persons who are currently eligible for a deduction) would be treated in the same way as contributions made for the benefit of employees. That is, the self-employed would be able to claim a full deduction for all contributions made to accumulation schemes on their own behalf up to age 75.

Extension of the Government's co-contribution scheme to the self-employed, effective from 1 July 2007

Impact analysis

Benefits

Individuals (including the self-employed)

8.110 The increased deductibility of superannuation contributions and the Government co-contribution, coupled with the abolition of end benefits taxation and the reduced age pension assets-test taper rate would bring significant benefits to the self-employed.

8.111 A self-employed individual earning $28,000 and contributing $2,500 per annum to superannuation over a working life of 40 years would be expected to have an increase in their benefit at retirement of over $88,000 or $113 per week if they took their benefit as a superannuation pension.

8.112 A self-employed individual with less time remaining in the workforce would still stand to gain considerably under the proposed incentives. A self-employed individual earning $90,000 and contributing $12,000 to superannuation per annum over a working life of 20 years would be expected to have an increase in their benefit at retirement of over $83,000 or $160 per week if they took their benefit as a superannuation pension.

8.113 Consultation with industry suggests that self-employed people who currently seek professional advice on superannuation are likely to seek less advice as a result of the proposed changes, saving an average of around $50 each per year.

Other

8.114 Employers, superannuation funds and the Government would not receive additional benefits.

Costs

Other

8.115 Individuals, employers, superannuation funds and the Government would not incur additional costs.

Recommendation

8.116 It is recommended that the self-employed be allowed full deductibility for their contributions to superannuation and given access to the Government's co-contribution scheme. These amendments will address the inequities of the existing arrangements for the self-employed, improve retirement incomes and provide cost savings for the self-employed.

Improvement and simplification of the arrangements to find, transfer and consolidate lost superannuation

Problem identification

8.117 Since 1 July 2004, members of most superannuation funds have been able to move their superannuation benefits into a fund of their choice (portability), subject to some limited exceptions.

8.118 Portability is further complemented by the Lost Members Register maintained by the ATO. The Lost Members Register contains details of accounts that individuals may have lost track of (the actual money remains with the relevant funds). Individuals who may have lost track of their superannuation can search the Lost Members Register (for free) to identify their accounts, and then, using portability, organise for those accounts to be consolidated if desired. At 30 June 2005, the Lost Members

Register held records of approximately 5 million accounts with a total value of around $8 billion.

8.119 The Government's initiatives on choice and portability have significantly improved the ability of individuals to manage and take control of their superannuation.

8.120 However, the Government considers there is scope to make transferring and consolidating accounts simpler and easier by further improving the operation of the portability and Lost Members Register arrangements.

- The absence of standardised portability documentation imposes unnecessary administrative costs on superannuation funds as they are often required to seek additional information from members when processing a transfer application.

- The 2005 Australian National Audit Office audit report on the ATO's administration of the Lost Members Register found that while the ATO has implemented strategies and mechanisms to promote awareness of, and enable access to, the Lost Members Register, an evaluation of the effectiveness of its strategies and tools to reunite people with their lost superannuation would be timely.

- Improvement and simplification of the arrangements to find, transfer and consolidate lost superannuation may ultimately reduce the number of accounts on the Lost Members Register by encouraging individuals to increase their engagement with their superannuation.

Options

A staged approach to address the number of lost accounts would be adopted

8.121 The process would commence in 2006 07 with a rationalisation and improvement of existing processes for lost member identification and the introduction of a standardised portability form. The maximum time period in which a transfer must occur would be reduced from 90 days to 30 days.

ATO to contact lost members

8.122 In 2007-08, the ATO would move to a more proactive role by contacting lost members by phone and mail. This would include targeting members with small balances to facilitate direct repayment or consolidation with an active account utilising the standardised portability form.

8.123 By 2009-10, members would be able to electronically request consolidation of their accounts via a facility on the ATO's website.

Impact analysis

Benefits

Individuals (including the self-employed)

8.124 The development of a standardised portability form would facilitate account consolidation, and would reduce the need for individuals' direct involvement.

8.125 Requests for account transfers would be processed more quickly, increasing the likelihood that individuals' superannuation assets would be held in accounts that reflect their immediate preferences (eg, fees and charges and level of insurance coverage).

8.126 Streamlining the portability arrangements would encourage individuals to claim and consolidate their accounts, eliminating multiple fees and charges and allowing individuals to claim the full entitlement of their accumulated superannuation benefits in retirement.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.127 The use of a standardised portability form and proof of identity requirements would potentially reduce the need for funds to seek additional information from members, thereby decreasing the costs of processing a transfer application.

Government

8.128 Over time, the ATO would have lower administration costs through a reduction in the number of accounts listed on the Lost Members Register.

Other

8.129 Employers would not receive additional benefits.

Costs

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.130 Some funds may be required to update their existing administrative systems (both electronic and manual) to meet the 30-day rule.

Government

8.131 The ATO would require additional resourcing to manage the increased administrative workflow resulting from greater efforts to reunite lost members with their superannuation.

Other

8.132 Individuals and employers would not incur additional costs.

Recommendation

8.133 It is recommended that the proposed staged approach to improving the portability and Lost Members Register arrangements be adopted. The amendments will provide individuals with substantial ongoing compliance savings which will significantly outweigh the initial implementation and ongoing compliance costs of superannuation funds and the costs stemming from the ATO's increased administrative workflow.

Improvement of self-managed superannuation fund compliance

Problem identification

8.134 The Government is concerned at the level of compliance with superannuation law by self-managed superannuation funds and the level of trustee education and their understanding of their responsibilities.

8.135 Approved auditors operate as a key integrity element in the regulation of self-managed superannuation funds by providing independent assurance that a self-managed superannuation fund is complying with its regulatory obligations. However, there are concerns with the oversight being provided by approved auditors.

8.136 A survey by CPA Australia found that 30 per cent of self-managed superannuation fund members do not realise they are also a trustee of their fund. A lack of awareness results in higher levels of non-compliance, risks the fund being declared non complying and puts members' retirement incomes at risk.

8.137 The current penalty regime for self-managed superannuation funds does not provide sufficient flexibility for the ATO in administering the law.

8.138 Currently if an *in specie* contribution (eg, business real property or shares) is made to a fund by an employer for the benefit of an employee, the employer may incur a fringe benefit tax (FBT) liability. A contribution made by a payment of money that meets certain conditions is specifically excluded from FBT.

8.139 The Financial System Inquiry recommended that '… as far as practicable, the regulatory agencies should charge each financial entity for direct services provided, and levy sectors of industry to meet the general costs of their regulation'. The current $45 self-managed superannuation fund levy has not changed since 1999 and no longer adequately covers the cost of the ATO's regulation of self-managed superannuation funds. The current supervisory level for small (less than five members) Australian Prudential Regulation Authority regulated funds is $500.

Option One: Improvement of regulatory processes within existing frameworks

8.140 This approach would include:

- simplifying self-managed superannuation fund reporting requirements by replacing the current requirement for multiple reports with a single annual report;
- making the Auditor Contravention Report an approved form;
- improving the level of education and assistance provided by the ATO to self-managed superannuation funds trustees;
- introducing additional legislative changes to assist in the prevention and management of compliance problems in self-managed superannuation funds; and
- removing the application of FBT to in specie transfers of assets to superannuation funds.

8.141 Option One would also involve the provision of additional funding for the ATO to regulate self-managed superannuation funds by raising the supervisory levy to $150 (see cost recovery impact statement in paragraphs 8.185 to 8.208).

Impact analysis

Benefits

Employers

8.142 Employers would benefit from not having to pay FBT on in specie contributions made on behalf of their employees.

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.143 Simplified reporting requirements would make it easier for self-managed superannuation fund trustees to meet their

compliance obligations, potentially reducing the costs of compliance.

8.144 The increase in direct costs resulting from the rise in the supervisory levy would be partially offset by a decrease in compliance costs through streamlined and more efficient collection processes. The supervisory levy would be collected at the same time as the fund's income tax liability.

8.145 Using the Business Cost Calculator, the simplified arrangements are estimated to produce an average compliance saving of $80 per annum for each self-managed superannuation fund.

Government

8.146 The appropriate level of regulation would enhance self-managed superannuation fund compliance while maintaining freedom and flexibility — key priorities of Australia's retirement income policy. A standard Auditor Contravention Report would improve communication between auditors and the ATO, allowing auditors to quickly and easily alert the ATO to incidences of non compliance.

8.147 Option One would provide the ATO with additional tools to enforce self-managed superannuation fund compliance (eg, the application of administrative penalties where self-managed superannuation funds fail to lodge returns or make false or misleading statements).

8.148 The rise in the supervisory levy would allow the ATO to broaden its self-managed superannuation fund compliance activities, ensuring the integrity of the proposed limits on contributions. The broadening of the ATO's education activities would assist the ATO in ensuring that self-managed superannuation fund trustees understand their obligations and responsibilities.

8.149 The ATO's estimated costs of regulating self-managed superannuation funds are based on total costs over the forward estimates period. The estimated costs would be broadly offset by the collection of the supervisory levy, and an improved rate of collection, over the same period.

8.150 The revenue impact of the increase in the supervisory levy is estimated to be $55 million over the forward estimates period.

Other

8.151 Individuals would not receive additional benefits.

Costs

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.152 The increase in the supervisory levy would increase a self-managed superannuation fund's direct costs by $105 per annum. However, ATO data suggests that the annual cost of running a self-managed superannuation fund ranges from around $1,500 to $12,000 for larger funds. In this context, an increase in the levy of $105 per annum would not add significantly to the running costs of a self-managed superannuation fund.

8.153 Administrative penalties for the late or non-payment of the levy would also increase direct costs.

Government

8.154 The ATO may need additional resourcing to implement the more direct supervisory activities envisaged in Option One.

8.155 The Government may experience a very minor decline in revenue as a result of the proposal to exempt in specie contributions from FBT, although this cannot be quantified.

Other

8.156 Individuals and employers would not incur additional costs.

Option Two: Introduction of new rules

8.157 This approach would include:

- requiring self-managed superannuation funds to have a third party independent trustee who would be required to sign off on all decisions and transactions of the fund;

- setting a minimum balance before individuals can establish a self-managed superannuation fund; and
- tightening self-managed superannuation fund investment rules, including limiting the classes of assets in which self-managed superannuation funds are allowed to invest.

Impact analysis

Benefits

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.158 Self-managed superannuation fund trustees may find it easier to comply with well-defined and tightly regulated rules. Option Two would provide trustees with a degree of protection, as the requirement for an independent trustee may reduce the possibility of the self-managed superannuation fund inadvertently breaking the law.

Government

8.159 The introduction of more prescriptive rules would facilitate the ATO's administration of self-managed superannuation funds.

Other

8.160 Individuals and employers would not receive additional benefits.

Costs

Superannuation funds (including approved deposit funds, RSA providers and self-managed superannuation funds)

8.161 The degree of flexibility currently afforded to self-managed superannuation fund trustees would be significantly reduced.

8.162 Compliance costs (in terms of both time and money) would be expected to increase through the requirement to employ an independent trustee.

Government

8.163 The ATO would require additional resourcing to update its self-managed superannuation fund administration systems.

Other

8.164 Individuals and employers would not incur additional costs.

Recommendation

8.165 It is recommended that Option One be adopted.

8.166 The range of proposals identified in Option One are preferable to those identified in Option Two, as the benefits expected from Option One are greater than those for Option Two and the associated costs would be less.

- Option One will provide the Government with more certainty over the regulation of self-managed superannuation funds and their compliance with superannuation law, without compromising freedom and choice.
- Increased funding for the ATO's self-managed superannuation fund supervisory activities will enable the ATO to more efficiently and effectively regulate self-managed superannuation funds and target problem funds.
- The education initiatives proposed in Option One will improve community awareness and understanding of the laws relating to self-managed superannuation funds, reducing the likelihood of unintentional non-compliance and reinforcing the integrity of retirement income policy.

Estimates of compliance costs and compliance savings

8.167 Table 8.1 details the ATO's estimates of net potential compliance costs and compliance savings from *Simplified Superannuation*.

8.168 The implementation and on-going compliance costs and compliance savings identified in the table relate to the key policy proposals discussed above, along with minor policy proposals, transitional and administrative arrangements which are not separately identified in this regulation impact statement.

Table 8.1

	Implementation savings/(costs) $ million	***Ongoing savings/(costs) $ million per year***
Individuals*	(10.7)	76.0
Employers**	(29.4)	8.7
Funds (including self-managed superannuation funds)***	(180.6)	32.2

* Key implementation costs for individuals relate to learning and education. These compliance costs are expected to be offset by ongoing compliance savings generated from the abolition of end benefits tax, RBLs, and improved arrangements to find and transfer superannuation.

** The implementation costs for employers reflect only the proposed changes to employment termination payment rules, which mainly affect large companies (see paragraphs 8.14 to 8.54). It is expected that these compliance costs would be offset by ongoing compliance savings from the streamlined arrangements for employment termination payments.

*** Key implementation costs for superannuation funds relate to a need to review and adapt record-keeping systems and processes (both electronic and manual), particularly in relation to the proposed arrangements for the quotation of TFNs (see paragraphs 8.55 to 8.74); learning and education; and advice and planning. These compliance costs are expected to be offset by ongoing compliance savings generated from the abolition of end benefits tax, RBLs, streamlined pension rules, and, for self-managed superannuation funds, streamlined reporting requirements.

8.169 The Government will provide additional funding of $500 million over the next four years to the ATO, Department of Families, Community Services and Indigenous Affairs, Centrelink and Department of Veterans' Affairs to administer the *Simplified Superannuation* reforms.

8.170 Estimates of potential compliance costs and compliance savings are based on assumptions about the time taken and level of expertise required to perform compliance tasks under both the current system and the proposed arrangements. The estimates are therefore sensitive to changes in these assumptions.

Fiscal impact

8.171 Taken together, *Simplified Superannuation* is expected to result in an aggregate fiscal cost of $7.2 billion over the forward estimates (including administration costs). As noted in paragraph 8.54, the abolition of the tax on contributions would result in a significantly higher cost to revenue.

Consultation

8.172 The Government has undertaken extensive consultation with a range of employer, consumer, industry and professional groups since the announcement of A Plan to *Simplify Superannuation* on Budget night, 9 May 2006. In addition to delivering numerous presentations and attending meetings across Australia, Treasury officials participated in forums with independent groups.

8.173 Industry bodies consulted by Treasury during the three-month consultation period include: AMP; Association of Independent Retirees; Association of Superannuation Funds of Australia; Association of Tax and Management Accountants; Australian Bankers Association; Australian Chamber of Commerce and Industry; Australian Institute of Superannuation Trustees; Business Council of Australia; Chartered Professional Accountants Australia; Corporate Superannuation Association; Council of Small Business Organisations of Australia; CPA Australia; EquipSuper; Financial Planners Association; Industry Funds Forum; Institute of Actuaries of Australia; Institute of Chartered Accountants of Australia; Investment and Financial Services Association; Law Council of Australia Superannuation Committee; Mercer Human Resources Consulting; National Institute of Accountants; Small Independent Superannuation Funds of Australia; Self-Managed Superannuation Fund Professionals Association of Australia; Taxation Institute of Australia; and Taxpayers Association of Australia.

8.174 Key stakeholders expressed strong support for the key elements of *A Plan to Simplify and Streamline Superannuation* on the basis that they will simplify the administration of superannuation, provide retirees with greater flexibility, improve incentives to work and save, decrease costs and enhance the operation of the superannuation system. The bulk of the feedback received by the Government centred on administrative, operational and transitional issues.

8.175 Community members were also given the opportunity to make comments and submissions on *A Plan to Simplify and Streamline Superannuation* through the 'Simpler Super' email service and the Superannuation Hotline. At the conclusion of the consultation period on 9 August 2006, the Simpler Super service had received 1,127 emails while the Superannuation Hotline received 3,645 telephone enquiries.

8.176 The views expressed by stakeholders and members of the community during the three month consultation period were examined and considered by the Government. Overall, the Government received over 1,500 submissions and comments on the plan. The main issues raised in submissions related to the contribution rules and their associated administration, the parity of the proposed treatment of benefits paid from taxed and untaxed sources and the taxation of death benefits for non dependants. Issues outside *A Plan to Simplify and Streamline Superannuation* were also raised, including the work test in relation to contributions made by persons aged 65 or over, full deductibility for all contributions and commutation of complying income streams.

8.177 The feedback received by stakeholders and members of the community resulted in a number of changes to the reforms proposed in *A Plan to Simplify and Streamline Superannuation*, which have been reflected in the Government's final policy decision, *Simplified Superannuation*. For example:

- The plan did not propose indexation of the limit on concessional contributions and the cap on non-concessional contributions. Industry argued strongly that the limit and cap should be indexed over time.
  - *Simplified Superannuation* would permit indexation of the limit and cap in $5,000 increments.

- A number of concerns were raised regarding the level of the cap on non-concessional contributions. Key stakeholders and members of the community sought the introduction of averaging provisions and requested consideration of certain exemptions.
  - *Simplified Superannuation* would allow individuals under age 65 to make larger non-concessional contributions of up to $450,000 by bringing forward two years of future entitlements. Moreover, the proceeds from the disposal of small business active assets up to $1 million and permanent incapacity payments would be excluded from the cap.
  - As a transitional measure, *Simplified Superannuation* would allow individuals who meet the work test to contribute up to $1 million in post-tax contributions between 10 May 2006 and 30 June 2007 irrespective of future work status.
- The plan proposed to remove the existing portability retriggering provisions so that in all cases benefits would be transferred within 30 days of a transfer request (the retriggering provisions allow the current 90-day rule to start again if a fund is required to seek additional information from a member). Industry expressed a preference for the 30-day rule to commence upon receipt of all information required to process a transfer request.
  - Under *Simplified Superannuation*, the 30-day rule would commence upon receipt of a valid and complete transfer form, consistent with industry's preferred approach.
- The plan did not propose to alter the treatment of invalidity benefits paid to the self-employed. However, during the consultation period, industry expressed concern that employees invalided out of the workforce receive part of their lump sum tax free, whereas the self-employed are unable to access this concession due

to the requirement for the termination of employment under current law.

– Under *Simplified Superannuation*, lump sum invalidity benefits paid to the self-employed would receive the same concessional tax treatment afforded to employees.

Conclusion

8.178 *Simplified Superannuation* encompasses all of the recommended options in this statement. Taken together, these options will enhance the fairness, integrity and equity of the superannuation system, and create more opportunities for individuals to work and save.

8.179 The reforms will simplify and streamline the existing superannuation system, generating substantial improvements and savings for individuals, employers, superannuation funds and the Government at the lowest cost.

Implementation and review

8.180 *Simplified Superannuation* will commence on 1 July 2007, with the exception of:

- abolition of compulsory withdrawal (10 May 2006);
- reduction in the pension assets-test taper rate and related changes (20 September 2007); and
- transitional cap and exemptions for non-concessional contributions (10 May 2006).

8.181 Press Release No. 093 of 5 September 2006, issued jointly by the Treasurer and the Minister for Revenue and Assistant Treasurer, announced *Simplified Superannuation*.

8.182 Following consultation with industry, the implementation arrangements for the treatment of excess concessional contributions were modified (see paragraphs 8.57 to 8.60). Under *A Plan to Simplify and Streamline Superannuation*, contributions in excess of the concessional cap would be taxed at the top marginal

rate and the ATO would raise a tax assessment on the fund. However, industry expressed concern that this approach would impose significant administrative costs on funds. Under *Simplified Superannuation*, the additional tax payable on concessional contributions in excess of $50,000 will be levied on the individual who can then direct their fund to pay the tax. This approach will minimise compliance costs for superannuation funds.

8.183 The Government will continue to consult with peak representative bodies such as Association of Superannuation Funds of Australia and Investment and Financial Services Association regarding the implementation of *Simplified Superannuation*.

8.184 *Simplified Superannuation* will be subject to ongoing review by the administering agencies.

Cost recovery impact statement

Purpose

Improvement of self-managed superannuation fund compliance.

8.185 Since 1991 all superannuation funds, including self-managed superannuation funds, have been subject to a supervisory levy designed to fund the regulatory costs of ensuring funds comply with superannuation legislation.

8.186 This approach was confirmed as appropriate by the 1997 Financial System Inquiry which recommended that '… as far as practicable, the regulatory agencies should charge each financial entity for direct services provided, and levy sectors of industry to meet the general costs of their regulation'.

8.187 Cost recovery of general regulatory oversight continues to be considered appropriate for the entire superannuation industry. Since 1999 regulatory responsibility for superannuation funds has been split between the ATO (responsible for self-managed superannuation fund regulation) and the Australian Prudential Regulation Authority (APRA) with separate levy arrangements applying to self-managed superannuation fund and APRA regulated funds.

8.188 This statement proposes a material amendment to the cost recovery arrangements for self-managed superannuation funds to ensure that amounts collected are broadly sufficient to fund the expected ongoing costs of effective ATO regulation. Specifically, it is proposed that the existing self-managed superannuation fund supervisory levy be raised from $45 to $150.

8.189 The proposed amendment would be implemented as part of a package of reforms envisaged under *Simplified Superannuation*, announced by the Government on 5 September 2006. This statement is intended to be read in conjunction with the rest of the regulation impact statement for the reforms.

Background

8.190 The ATO assumed primary responsibility for the supervision of self-managed superannuation funds in October 1999. Its regulatory role is currently exercised through the *Superannuation Industry (Supervision) Act 1993* and the *Superannuation Industry (Supervision) Regulations 1994*. The ATO is tasked with ensuring that self-managed superannuation fund trustees comply with their legislative obligations under this legislation. Obligations under this legislation include requirements to lodge returns, comply with rules on superannuation contributions and benefit payments, and comply with rules on superannuation investments.

8.191 Prior to 1999, the supervisory levy paid by self-managed superannuation funds was set at $200 per annum. The levy was reduced when the ATO assumed responsibility for self-managed superannuation funds, as it was considered that the $200 levy would exceed the costs of the ATO's regulation.

8.192 The current supervisory levy imposed on self-managed superannuation funds is $45 per annum. This amount has not been changed since 1999 and no longer covers the cost of the ATO's regulation of self-managed superannuation funds nor the expected costs of future regulation. The shortfall between the amount levied and the ATO's regulatory costs has, to date, been subsidised from general tax revenue.

Australian Government cost recovery policy

8.193 In December 2002, the Australian Government adopted a formal cost recovery policy to improve the consistency, transparency and accountability of its cost recovery arrangements and promote the efficient allocation of resources. Cost recovery policy is administered by the Department of Finance and Administration and outlined in the *Australian Government Cost Recovery Guidelines* and the Review Schedule is outlined in *Finance Circular 2005/09*. Cost recovery broadly encompasses fees and charges related to the provision of Government goods and services (including regulation) to the private and other non-government sectors of the economy.

8.194 The policy applies to all *Financial Management and Accountability Act 1997* agencies and to relevant *Commonwealth Authorities and Companies Act 1997* bodies that have been notified, under section 28 or 43 of the *Commonwealth Authorities and Companies Act 1997*, to apply the cost recovery policy. These entities are collectively referred to as 'agencies' for the purposes of the guidelines. In line with the policy, individual portfolio ministers are ultimately responsible for ensuring agencies' implementation and compliance with the cost recovery guidelines.

Policy review — analysis of activities

Description of activity

8.195 It is proposed that the current supervisory levy be increased from $45 per annum to $150 per annum to reflect the expected costs of ATO regulation. While the increased levy would take effect from the 2007-08 financial year, revenue will not be received until the 2008-09 financial year.

8.196 The process for collection of the levy would also be streamlined, by incorporating the levy into self-managed superannuation fund income tax assessments. Currently, the levy is collected by a separate process whereby the ATO issues an invoice to each self-managed superannuation fund for payment.

Analysis of costs and benefits

Self-managed superannuation funds

8.197 The increase in the supervisory levy would increase a self-managed superannuation fund's direct costs by $105 per annum. However, ATO data suggests that the annual cost of

running a self-managed superannuation fund ranges from around $1,500 up to almost $12,000 for larger funds. In this context, an increase in the levy of $105 per annum would not add significantly to the running costs of a self-managed superannuation fund.

8.198 In addition to improving the effectiveness of ATO compliance activities, the increased funding will also enable the ATO to broaden its education activities which will assist self-managed superannuation fund trustees to understand their obligations and responsibilities.

Government

8.199 The provision of additional funding would allow the ATO to broaden its self-managed superannuation fund compliance activities and more effectively ensure self-managed superannuation funds are complying with their legislative obligations. This is especially important in the context of the growing number and size of such funds.

8.200 The revenue impact of the increase in the supervisory levy is estimated to be $55 million over the forward estimates period.

Table 8.3: Impact on the underlying cash balance of the increase in the supervisory levy

	2006-07 ($m)	***2007-08 ($m)***	***2008-09 ($m)***	***2009-10 ($m)***	***Total ($m)***
Increase in supervisory levy	–	–	+24.0	+31.0	+55.0

Conclusion

8.201 It is recommended that the current supervisory levy be increased from $45 per annum to $150 per annum, to better reflect the cost of the ATO's self-managed superannuation fund supervisory activities.

Design and implementation

Basis of charging — fee or levy

8.202 Cost recovery of the ATO's self-managed superannuation fund supervisory activities through the imposition of a levy has been in place for a number of years. The levy remains the most efficient and effective mechanism for cost recovery.

Legal requirements for the imposition of charges

8.203 Supervisory levies are currently imposed on all superannuation funds, including self-managed superannuation funds. The legislative authority for imposing a levy on self-managed superannuation funds is provided by the *Superannuation (Self Managed Superannuation Funds) Supervisory Levy Imposition Act 1991*.

Outline of charging structure

8.204 For simplicity, the levy will be applied at a flat rate of $150 per self-managed superannuation fund (consistent with current arrangements). The ATO will manage under-over-recoveries over the medium term. Sustained under-recoveries will be managed through an amendment to the levy to reflect the higher costs of supervision; while sustained over recoveries will be returned to the industry via reduced charges.

8.205 Detailed analysis of the ATO's costs of self-managed superannuation fund regulation was taken into consideration in identifying the appropriate levy.

Ongoing monitoring

Monitoring mechanisms

8.206 The ATO would implement an ongoing monitoring process to assess the efficiency and effectiveness of levy collections. This process would reflect the Government's cost recovery guidelines and would ensure the ongoing appropriateness of the levy charged, by periodically assessing the size of the levy with the costs incurred by the ATO in discharging its self-managed superannuation fund supervisory responsibilities. This process

would provide an opportunity for continual improvement of the levy collection arrangements.

Stakeholder consultation

8.207 This statement proposes an increase in the quantum of the existing levy to reflect necessary costs incurred to ensure effective regulation, rather than wholesale changes to the arrangements for cost recovery. As a result, consultation was not considered necessary.

Periodic review

8.208 The ATO will also review the levy collection arrangements and the adequacy of monitoring processes no later than 30 June 2011 to ensure the levy continues to provide appropriate cost recovery of the ATO's functions. The review will be undertaken in accordance with Australian Government cost recovery policy and a cost recovery impact statement will be prepared. The purpose of the review will be to ensure that the supervisory levy collected from self-managed superannuation funds accurately reflects the ATO's regulatory costs over the medium term.

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