



THE TAX INSTITUTE
THE MARK OF EXPERTISE

21 February 2017

Ms Jenny Wilkinson
Division Head
Superannuation Tax Reform
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: superannuation@treasury.gov.au

Dear Ms Wilkinson,

Superannuation Reform Package - Regulations

The Tax Institute welcomes the opportunity to make a submission to the Treasury in relation to the draft regulations and associated explanatory material relating to the superannuation reform package (**Reforms**).

Summary

Our submission below addresses our main concerns in relation to the Reforms. In particular:

- 1. Objective of the superannuation system** — The Tax Institute would welcome additional text from the Explanatory Statement, which elaborates on the objective of the superannuation system, being added into the regulations.
- 2. Transition to retirement income streams (TRIS)** — capital gains tax (**CGT**) relief should be available for members with a TRIS.
- 3. Excess Transfer Balances** — in our view, it would be helpful if further clarity is provided to explain when a capped defined benefit income stream can be commuted. It would also be helpful if further clarity is provided on the process of how a member advises a trustee of a superannuation fund of an expected excess and how the trustee should consider the reasonableness of such a request.

Discussion

1. Objective of the superannuation system

The Tax Institute appreciates that the secondary objectives to “facilitate consumption smoothing over the course of an individual’s life” and to “manage risks in retirement” are compatible with the support and development of lifetime pension and other longevity risk insurance products in superannuation that have been a focus of recent Government reviews into superannuation.

However, The Tax Institute submits that more explicit reference should also be made to the role of insurance products in superannuation that provide death and permanent and temporary incapacity benefits to support ongoing living costs. In addition, the proceeds of these policies are not just necessary to support the individual, but also to support dependant family members.

The Tax Institute reiterates its view expressed in previous submissions that the primary objective of superannuation should be to provide a comfortable standard of living in retirement for the individual and dependant family members. The current proposed primary purpose of superannuation, which is to be a substitute or supplement for the Age Pension, is setting the bar too low. The Tax Institute would welcome additional text from the Explanatory Statement, which elaborates on this objective being added into the regulation itself (i.e. that the superannuation system should “increase self-reliance” and “assist individuals improve their standard of living in retirement”).

2. CGT relief

A key legislative shortcoming in the superannuation reforms is that a superannuation fund cannot elect to apply the transitional CGT relief for members with a TRIS and income streams in excess of the \$1.6m transfer balance cap unless, in respect of the segregated method, the member takes action before 1 July 2017, rather than after. In the interests of simplicity and fairness for members that do not quickly become fully aware of the minutiae and full ramifications of the superannuation tax changes, the CGT election deadline should be extended to at least 30 June 2018.

We are aware of situations where some advisers are fully booked up until 30 June 2017. This means that some advisers may not be able to provide advice on decisions their clients need to make before 1 July 2017. We recommend at least a 12-month period leading up to 30 June 2018 for the community and advisers to be educated about the transitional CGT relief and for any election to be made.

This makes sense as there would be 12 months from 1 July 2017 for SMSF trustees to obtain advice and make their election.

3. Definition of TRIS

As a related aspect that can be addressed in the Superannuation Industry (Supervision) regulations, consideration should be given to amending the definition of TRIS so that an account-based pension that is started as a TRIS ceases to be a TRIS once the superannuation fund becomes aware that a full condition of release has occurred (e.g., retirement after preservation age or otherwise satisfying regulation 6.01(7) that converts the member's benefits into unrestricted non-preserved benefits). That would mean that members who started a TRIS, but have already reached age 65 (or met some other condition of release with a nil cashing restriction that the fund is aware of) would not need to take action before 1 July 2017 to stop and restart their income stream. The member could then lodge the relevant forms with the ATO.

Thus a member could simply notify the fund trustee of any change, access to their super or allow the change in status to apply automatically at age 65.

Our members also have concerns regarding how the CGT relief will be applied to large funds. We recommend investigating other options. However, in this submission, we have focused on issues relating to self-managed superannuation funds.

4. Excess transfer balance

The proposed regulations allow certain otherwise generally non-commutable income streams to be partly commuted to avoid a transfer balance account excess that the member has or expects to have. It would be helpful if further clarity is provided in the Explanatory Statement to explain what criteria must be satisfied before a commutation of a capped defined benefit income stream can occur.

In this regard, we request guidance in the Explanatory Statement on:

- i) whether commutations in relation to market linked pensions and life expectancy pensions merely apply to those that are capped defined benefit income streams that were already in retirement phase just before 1 July 2017; and
- ii) whether the excess on any market linked pensions and life expectancy pensions would be able to be commuted.

Prima facie if every member was to utilise this process, there would be no need for the legislative provisions to tax the income from capped defined benefit income streams. Consideration of providing an option should be provided where a commutation could occur or members can decide to pay more tax. Nevertheless, we also seek clarity in the Explanatory Statement about the intended process by which the member would advise the fund trustee of the excess he or she expects to have and how the trustee can consider the reasonableness of the matter. Also clarity in the Explanatory Statement about whether there is any discretion for the trustee to reject such a request would assist.

It might also be helpful if a Law Companion Guide was prepared by the ATO to explain practically which non-commutable income streams would be able to be partly-commuted in this way, with particular focus on income streams commenced before 20 September 2007 (or purchased since then using rollover money from an earlier income stream that was generally non-commutable).

5. Definition of when a superannuation income stream is in the retirement phase

Commencing from 1 July 2017, it becomes crucial whether an income stream is in the retirement phase. Meeting this definition triggers reporting for the Transfer Balance Cap, the availability of exemption for the income of the fund and whether a pension is a permitted type of death benefit pension. The definition is contained in section 307-80 of the *Income Tax Assessment Act 1997* (Cth) (**1997 Act**). Of critical importance is the exclusion from the definition at paragraph 307-80(3)(a) of “a transition to retirement income stream (within the meaning of Part 6 of the *Superannuation Industry (Supervision) Regulations 1994* (Cth))”.

The Part 6 definition of “transition to retirement income stream” allows a pension to be commenced upon reaching preservation age, subject to certain conditions. The definition in Part 6 is concerned with the criteria for commencement of the pension. There is nothing in the definition that requires the criteria for a pension to cease and a new pension to commence when the criteria is satisfied.

In practice, when a pensioner meets a full or nil condition of release, the pension continues with the payment restrictions removed and this continuing nature is recognised as there is no need to make a pro-rata minimum payment. Similarly, where it is a reversionary pension and the original recipient dies, the minimum payment resets at the next 1 July, not at the death of the pensioner. It is a continuing pension obligation that exists under the criteria. It follows that it may, in effect, now just be an account-based pension because the TRIS criteria are no longer applicable.

We are therefore concerned that the law will not recognise existing transition to retirement pensions for members who have met a full condition of release as satisfying the retirement phase definition. We understand that for many industry and large superannuation funds it is common practice that the same pension has continued after the satisfaction of a full condition of release, such as retirement or attaining age 65 without any need of a pension reset.

We therefore recommend that the definition of a TRIS in Part 6 be amended so that a pension that is commenced as a TRIS ceases to meet that definition once a full condition of release is satisfied. We also recommend that the operative date for the pension to be the date of commutation. This will allow some flexibility to members and notify funds that the status of the pension recipient has altered.

6. Other changes

The Tax Institute welcomes the other changes in the proposed regulations, in particular the simplification of the release authority administrative processes.

If you would like to discuss any of the above, please contact either me or Tax Counsel, Angie Ananda, on 02 8223 0011.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Matthew Pawson', with a stylized, flowing script.

Matthew Pawson
President