SMSF
Owners'
Alliance
Limited ABN 96 161 052 464
Not-for-profit public company

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Superannuation Legislation
SMSF Owners' Alliance is an independent, not-for-profit advocate for the one million Australians who are trustees and members of self-managed superannuation funds. These people have grasped the opportunity to secure their financial independence in retirement so as not to rely on a publicly funded pension. Our members are angry and anxious regarding the implications for them and the superannuation system of the changes announced by the Government at the last Federal Budget.
In that Budget the Government announced three controversial changes to the superannuation system:
a) That the sum that can be transferred from an accumulation account into a pension account be capped at $1.6million (Transfer Balance Cap);
b) That the cumulative total of non-concessional contributions (i.e. those on which Australians have already paid tax) be limited to $500,000; and
c) That the annual concessional contribution (i.e. contributions that are made before tax is deducted) is reduced to $25,000.
It is agreed that a tax system should provide incentives for workers to save for their retirement and our superannuation system has provided that since it was introduced in 1915 when the progressive income tax system was introduced. It is as old as that system.
However, if there are to be limits on access to tax incentives the limit should be on the level of contributions not on the final balance. We are against capping final balances because it is penalising people's investment success. Capping contributions is accepted by serious economists as the most effective limit.
We are therefore against the introduction of a cap on balances that can now be moved into the tax-free pension account (Transfer Balance Cap). However, if such a cap is introduced it does not make sense to also introduce a $500,000 limit on non-concessional contributions. Additionally, if a 'cap' is to be used it should be sufficient to achieve the objectives. Independent modelling by Dr Ron Bewley (ex-Professor of Econometrics and Head of the School of Economics at UNSW) indicates that $1.6million is totally insufficient. Other commentators have pointed out that even if the old Reasonable Benefit limit was reinstated and rolled forward the 'cap' would now be in excess of $2.5million.
Finally, our independent analysis has also demonstrated that the existing $30,000 limit on concessional contributions is already too low and so see the proposed reduction of this to $25,000 as a retrograde step and certainly it does nothing to improve the adequacy of the superannuation system. At a minimum this should be doubled for those over 50 who are trying to save enough for retirement.
None of the above measures improve the effectiveness or fairness of super. However, the worst aspect of the Budget proposals is the retrospectivity of the first two caps. Because superannuation is a very long-term savings system changes must only be made after careful deliberation and consultation and not to fix a budget deficit caused by excess spending. Both major parties have historically respected the decisions taken in good faith by existing savers and grandfathered them from any major changes. UNTIL NOW!
The Government has argued that the Transfer Balance Cap is not a new tax – it is just a limit on how much one can transfer from a taxable accumulation account, in which one's super is held whilst working, into a tax-free pension account, in which one's super is held during retirement. This may be technically correct but disingenuous.
The fact is that a new tax is being applied to earnings on savings in the retirement phase that did not exist before the Budget and, in fact, has never existed.
Retrospective unwinding of transfers that have already been made into pension accounts

Apart from applying this cap to future retirees, the Government proposes to backdate the Transfer Balance Cap so as to apply to transfers into pension account that have already been made legitimately under existing legislation.

1) There is no doubt that this is retrospective; such transfers have already been made legitimately and the Government proposed that some of this transfer must now be reversed;

2) It breaches the social contract between the Government and savers – the Government has legislated that if you forego spending during your working life, put money into super according to the rules then it will not be taxed in your retirement; and

3) On any independent analysis the $1.6million cap is insufficient to fund a pension likely to last 20 t0 30 years at anything like the equivalent of the stated Budget objective of 4 times the age pension or the equivalent of a public sector defined benefit pension of $100,000.

The introduction of this retrospectivity is not only contrary to the principles the Senate applies in assessing taxation legislation; it introduces complexity - and therefore more cost - and uncertainty into the superannuation system for all Australians.

The retrospective nature of The Transfer Balance Cap has not had as much negative publicity as the retrospective $500,000 cap on non-concessional contributions. This is perhaps because it has been reported that only a small percentage of people will be affected. Such claims by the Government are not only wrong (the percentage they have quoted is incorrect) but appears to demonstrate a complete lack of understanding of how the financial system and superannuation in particular works.

Trust and credibility are very important aspects of any effective financial system. This is particularly true for superannuation which is a very long-term savings system that requires people to make decisions regarding their level of consumption vs savings whilst working based upon an understanding of the long-term taxation of such savings. If implemented without amendment, this proposal will have dramatic and long-lasting impact on the credibility and stability of the superannuation system for all Australians.

Some issues that must be addressed in the legislation if this proposal is to be implemented are described in Appendix A.

Even if the Transfer Balance Cap is not to be applied retrospectively, there are many issues that must be addressed in legislation, some of which we have described in Appendix B.

Backdating the application of the new $500,000 limit on non-concessional contributions

It appears that the Government acknowledges that some people may not be able to save adequately through concessional contributions and so allow non-concessional ("tax-paid") contributions to be made to boost their savings in super. The Transfer Balance Cap then limits the total sum in each individual's pension account, so it does not seem obvious why the Government also thinks it needs to apply another $500,000 cap on the "Tax-paid" contributions.

Some of the issues that arise from such a retrospective application have already been addressed by the Government and we hope will be correctly legislated.

We clearly believe that, even if the Government retains this new limit, it should apply to contributions from 3 May 2016, Budget night. We are aware of members who are nearing retirement and whose major life decisions based upon the existing legislation have been disrupted by the sudden and unexpected backdating of this new limit. Such people will be unfairly impacted by this proposal vs other Australians who may have many more years before retirement.

If the Government insists on introducing the retrospectivity, we propose, at a minimum, that it does not apply to Australians who are within 10 years of retirement i.e.over 55.

A further issue which should be addressed in legislation is covered in Appendix C

We appreciate that superannuation, particularly as it affects self- funded (SMSF) retirees, is not well understood. It is therefore an area where policy changes, such as those proposed by the Government, should be carefully considered as otherwise unfair and unintended consequences will result.

We would be pleased to discuss this further with you at your convenience. Please call either the undersigned on 0411551855 or our Executive Director – Duncan Fairweather on 0412256200.

Yours sincerely,

Bruce Foy
Chairman

Appendix A

Retrospective issues with Transfer Balance Cap

1. Application of Transfer Balance Cap retrospectively

If the Government proceeds to include such retrospective application of the cap then it should ensure that the legislation does not unfairly penalise those who have already retired vs those yet to retire.

For many of these retired individuals, the sum they transferred into their pension account upon their retirement may well have been LESS than the $1.6million cap (even adjusting historically for CPI) but through careful investment now have MORE than $1.6m. The retrospective clawback of any excess funds now would penalise their prudent investment whereas such retrospective clawback will not be applied to those who have yet to retire.

We propose therefore that if the Transfer Balance Cap is to be applied retrospectively, it should be applied to the retrospective balance at the time the transfer was made into the pension fund. i.e. the CPI adjusted Transfer Balance Cap should be compared with the sum that this individual transferred into his or her pension account and the excess so calculated, if any, should be the sum he or she is now required to reverse the transfer and withdraw from the pension account.

2. Fairness between spouses

If it is intended that the Balance Cap applies per person then there will be circumstances when one partner in a couple has no super or a relatively lower amount and is relying on the main contributing partner to fund their retirement. An unintended consequence of the policy may be that one partner may be required to reduce his/her pension account by his/her Excess whilst his/her spouse has a balance that is below the Balance Cap. This would appear to be unfair to such couples relative to couples who have more equal balances in their super accounts.

It is most likely the disadvantaged partner will be a woman as it is common for women to have less superannuation because they often have less time in the workforce and lower pay rates than men.

We therefore propose that an individual may transfer out of his/her Taxable Pension Account into his/her spouse's Pension Account any amount, provided the balance of that spouse does not then exceed the Balance Cap.

3. Timing issues

The Budget stated that any excess in an existing pension fund that is over the cap as at 1 July 2017 must be withdrawn from the pension account.

There are two issues here. Funds are only audited as at one date in a year – 30 June. However, such audit may not be completed for a number of months.

So, the legislation must be clear that the Transfer Balance Cap is applied to balances as at 30 June 2017 as per audited accounts and any excess must be transferred before the end of the next financial year.

4. Minimum withdrawal

Furthermore, at present the minimum withdrawal in a year is calculated as a percentage of the balance on the previous 30 June. However, if a member is obliged to reduce such balance to the Transfer Balance Cap, the minimum withdrawal should apply to the reduced figure.

5. Taxation status re Transfers on death

Under existing superannuation legislation, the tax status of any super pension transferred to a spouse upon death of a member is retained.

We proposed that the legislation is clear that the current rules regarding transfers to spouses apply in that, following death of a member, a Pension Account transferred to a spouse under a binding death benefit nomination retains its tax-free status notwithstanding the size or status of that spouse's existing superannuation accounts.

Appendix B

Other issues with Transfer Balance Cap

1. Binding death benefit

Under a binding death benefit nomination, the surviving spouse's account may be below the indexed cap but the transfers to him/her may include an accumulation account.

We propose that a surviving spouse may top up his/ her pension account to the then Balance Cap using funds from a Taxable Pension Account transferred to him/her pursuant to a binding death benefit nomination.

2. Minimising increase in compliance costs

These proposals have already resulted in extra costs for superannuation funds in securing advice on what may need to be done to comply with the announced policy. There will also be future costs but the legislation should ensure unnecessary additional costs are minimised. The overall returns achieved from super funds and therefore their effectiveness as long-term savings vehicles are sensitive to the administrative cost burden.

At present, if the funds in a Self-Managed Superannuation Fund are either all in accumulation phase or all in pension mode there is no need to employ an actuary in addition to an auditor.

However, after the proposed changes are introduced, the fund may comprise both tax-free accounts and taxable accounts and under existing legislation, if assets cannot be segregated, an actuary must be employed to divide income between the two types of funds.

This computation is not complicated and we propose that in such circumstance the allocation of income between the funds is subject to audit but there is no requirement to also employ and pay for an actuary.

Appendix C

Issues with $500,000 Non-concessional Cap

It appears that the purpose of applying a non-concessional contributions cap as well as an overall Transfer Balance Cap is to limit the funds left in an accumulation account if the tax-free pension account is up to the limit.

However, due to the limits on concessional contributions and the constraints on an individual's ability to make concessional contributions, there may be individuals who have been unable to make adequate tax-deductible contributions during their working life, have reached the new non-concessional contributions cap BUT have NOT exceeded the Transfer Balance Cap. This appears to be an unintended consequence and unfair on those who have been unable to make adequate concessional contributions.

We propose therefore that on transfer of an accumulation account into a Pension Account upon retirement, notwithstanding that the non-concessional contributions cap has restricted any further non-concessional contributions, if the account balance is below the Transfer Balance Cap, an additional non-concessional contribution can be made equal to the gap between the account balance and the Transfer Balance Cap.

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