

28 October 2016

Superannuation Tax Reform
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: jessica.carew@treasury.gov.au

Dear Jessica

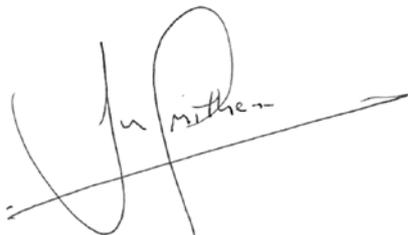
Consultation on the Superannuation reform package - tranche 3

I am pleased to enclose a submission prepared by the Superannuation Committee of the Legal Practice Section of the Law Council of Australia.

The Committee would welcome the opportunity to discuss the submission further. In the first instance, please contact:

- Ms Michelle Levy, Chair, Superannuation Committee (T) 02 9230 5170
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- Ms Heather Gray, Chair, Tax Subcommittee of the Superannuation Committee (T) 03 9603 3608 (E) heather.gray@hallandwilcox.com.au.

Yours sincerely



Jonathan Smithers
Chief Executive Officer



Law Council
OF AUSTRALIA

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The Treasury

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Acknowledgement

This submission has been prepared by the Law Council of Australia's Superannuation Committee (**the Committee**), which is a committee of the Legal Practice Section of the Law Council of Australia.

The Committee's objectives are to ensure that the law relating to superannuation in Australia is sound, equitable and clear. The Committee makes submissions and provides comments on the legal aspects of virtually all proposed legislation, circulars, policy papers and other regulatory instruments which affect superannuation funds.

About the Law Council of Australia

The Law Council of Australia exists to represent the legal profession at the national level, to speak on behalf of its Constituent Bodies on national issues, and to promote the administration of justice, access to justice and general improvement of the law.

The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian State and Territory law societies and bar associations and the Law Firms Australia, which are known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar
- Law Firms Australia
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of more than 60,000 lawyers across Australia.

The Law Council is governed by a board of 23 Directors – one from each of the constituent bodies and six elected Executive members. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive members, led by the President who normally serves a 12 month term. The Council's six Executive members are nominated and elected by the board of Directors.

Members of the 2016 Executive as at 1 January 2016 are:

- Mr S. Stuart Clark AM, President
- Ms Fiona McLeod SC, President-Elect
- Mr Morry Bailes, Treasurer
- Mr Arthur Moses SC, Executive Member
- Mr Konrad de Kerloy, Executive Member
- Mr Michael Fitzgerald, Executive Member

The Secretariat serves the Law Council nationally and is based in Canberra.

Submission

1. The Committee's response to the Superannuation reform package - tranche 3 (**Tranche 3**) is guided by its objectives as identified above.
2. The Committee has only made comments below where the Committee has identified issues within its remit, and has not been able, in the time available, to carry out a thorough review.

Preliminary

Consultation period

3. The Committee has previously commented in response to Tranche 2 of the draft legislation, and restates its concern with legal risks that arise:
 - with such a short consultation period on what is a very significant reform package requiring complex legislative changes;
 - with providing draft legislation for comment by way of "tranches", where such legislation and measures are not entirely self-contained and the position and approach taken with one set of measures may then impact on later tranches;
 - where subordinate legislation (regulations) are also key to the legal effectiveness of new measures and issues that arise in drafting those regulations may impact on the design or provisions of the statutory changes. It would be helpful for those draft regulations to be made available at the same time as the proposed legislative amendments.
4. In that context, the Committee welcomes the opportunity to continue to be consulted on the technical aspects of the legislation proposed and may provide further informed comment to Treasury, having regard to assessment of the three tranches as a whole.

Administration

5. The Committee notes that the legislation, as a whole, including the reduction to the annual non-concessional contributions (**NCC**) cap and interaction with an individual's total account balance being tested against the general transfer balance cap, will require individuals to track their total superannuation balance across all their superannuation interests in order to avoid inadvertent breaches of the new excess NCC cap measures.
6. These measures are inherently complex, but will need to be applied correctly by individuals who wish to make non-concessional contributions and to successfully use the "bring forward" facility. Such individuals will require accurate and 'real time' information to support them in taking such steps. The Committee submits that the Australian Taxation Office (**ATO**) should as a matter of public policy be required to inform individuals of their annual total superannuation interests and their personal transfer balance cap, and to warn individuals who it appears are likely to soon exceed the various caps, according to the ATO records held.

7. In essence, it should not be necessary for an individual to be required to incur costs in engaging an adviser in order to be able to:
 - understand the fundamental features of tax law that they will be required to comply with when saving for retirement; and
 - understand the extent to which they can contribute actively towards their retirement savings.

NCC caps

8. The Committee considers that the proposed regime under which different tests apply in determining an individual's ability to use the bring forward measure depending on the difference between the general transfer balance cap and the individual's total superannuation balance is unduly complex, and will lead to inadvertent breaches.
9. Not only are the rules difficult to follow, fund members may not always know their total account balances as at 30 June in any given year until some months later. Account balances may also be subject to adjustment as trustees address issues such as unit pricing errors, or the misallocation of contributions or other amounts.

Release Authorities

10. The Committee does not think that 7 business days is an adequate timeframe within which trustees should be required to action a release authority, and suggests that 10 business days would be a more reasonable period. The Committee notes that:
 - administrators are likely to require time to review and action release authorities outside of automated workflows;
 - it is common in the ordinary course of fund operations for short 'blackout' periods to apply, and
 - trustees may need to contact the affected member in order to seek instructions about matters such as the investment option from which the amount to be released should be taken.
11. Further, as per our comments on Tranche 2, the Committee considers that a clear and express "safe harbour" provision is required to protect trustees in dealing with release authorities – particularly where release authorities are mandatory, in the absence of instructions from the member.
12. Such trustees may need to make decisions about matters such as the investment option from which an amount is to be released. As a practical matter, it is unlikely that a trustee will be able to make such a decision based on an informed consideration of the affected member's circumstances. The trustee will not know, for example, whether the member has other interests in other superannuation funds, and how such amounts are invested, or the timeframe over which the member is likely to require access to their funds. In any event, the trustee's duty is to exercise its powers in the best interests of the beneficiaries as a whole and not on a member by member basis.
13. Provision should be made so that a trustee that complies with a mandatory release authority is protected where the trustee has in good faith adopted and applied a policy governing how these circumstances would be managed. Such a policy would be developed based on the interests of the beneficiaries of the fund as a whole. This is important to protect the trustee from claims and complaints where the trustee is

compelled to redeem a member's investments from a range of investment options to satisfy a release authority required at law and where no specific and valid member instructions have been received.

14. Under proposed section 131-15(2) of the *Taxation Administration Act 1953* the Commissioner may issue a release authority where an excess non-concessional contributions determination has been issued (or a notice has been issued in respect of such a determination under section 131-5(4)(b)) and the member has not made a valid request for the release of amounts in respect of that determination.

15. The Explanatory Material explains that:

10.30 The amendments also introduce a new circumstance in which mandatory release may occur - where the individual has excess non concessional contributions and has not notified the Commissioner about the amount that they want to be released.

10.31 Previously, if an individual did not make any election about the release of an amount upon receiving an excess non-concessional contributions determination, no amount would be released from their superannuation at that time.

10.32 This was almost always to the individual's detriment. If the amount is not released, the whole value of the contribution is subject to excess non-concessional contributions tax at a specified rate (generally 47 per cent in 2017-18). Further, as outlined above, the amount of this excess non-concessional contribution tax liability would then need to be released from the individual's superannuation interests.

10.33 Given the seriousness of this consequence, it is preferable that it only apply to an individual that has specifically chosen this outcome, rather than applying by default.

10.34 The amendments change this default position, allowing the Commissioner to release the amount of an individual's excess non concessional contributions in the absence of a request by the individual. [Schedule 10, Part 1, item 1, subsection 131-15(2)]

10.35 This position is only the default. An individual may still choose for no amount to be released by requesting the Commissioner not release any amount. This request will prevent the Commissioner from seeking the release of the full amount of the excess non-concessional contributions. However, it will not affect any subsequent mandatory release relating to the consequential excess non-concessional contribution tax liability.

16. Given this explanation, the Committee queries why the Commissioner should not be bound to issue a release authority in these circumstances? The Committee cannot readily envision circumstances in which the Commissioner would be in a position actively to exercise this discretion based on the individual's circumstances, but expects that the Commissioner would need to rely on the principle expressed above, which is that the non-release of the relevant amount from superannuation would be 'almost always to the individual's detriment'. On that basis, the Committee suggests that this provision should establish the new default position as per the Explanatory Memorandum, by requiring the Commissioner to issue a release authority in the circumstances described in proposed section 131-15(2) of the *Taxation Administration Act 1953*.

17. Further, the Committee notes that this default measure is intended to operate only in circumstances where the individual has not made an active choice - they have not notified the Commissioner of an amount to be released, being either nil (that is, they have actively determined that they want the relevant amount to stay in the superannuation system), or some other amount in accordance with section 131-10.

18. It will be important that individuals who receive an excess non-concessional contributions determination also receive information at that time that makes clear to them that they must make a request for a nil amount to be released if they are to avoid falling within the default position. The legislation as drafted does not make clear that a request under section 131-5 can include a 'nil' request, and the Committee submits that an ordinary (or even an expert) reader would not deduce from sections 131-5 and 131-10 that a person who did not want any amount to be released would as a practical matter have to make a request for the release of an amount, with the amount specified as nil.
19. At the least, the Committee recommends that section 131-5(2)(a) be amended to read:
- (a) notifying the Commissioner of the total amount to be released (which may be nil); and

Superannuation Guarantee

20. The Committee submits that the proposed changes to the NCC cap measures should cause Treasury to consider review of the superannuation guarantee (SG) legislation as it applies to individuals who will have SG contributions paid into superannuation only to then be required to have those amounts later released. The application of the \$1.6 million total account balance as an absolute cap beyond which there can be no further NCCs will make this issue more common for individuals who have significant superannuation savings and who receive SG contributions from numerous employers taking them above the \$25,000 concessional contribution cap. Those excess SG contributions will then be deemed to be NCCs.
21. The Committee raised this issue in its submission in respect of Tranche 2. The issue becomes more significant in light of the matters covered by Tranche 3.
22. The Committee acknowledges that there may not be substantial numbers of individuals affected by this scenario. However it would clearly be a 'reduction of red tape' measure to allow such individuals to opt-out of the SG system.
23. For simplicity and efficiency of the superannuation system, consideration might be given to whether it should be available to all individuals with a total superannuation account balance in excess of the general transfer balance account cap to opt-out of SG altogether.
24. A similar option was available to individuals when the SG legislation was introduced in 1992, but was changed following the 2007 'simpler super' reforms.

Special Circumstances

25. The Committee notes the proposal to apply the current relief mechanism under section 292-465 of the *Income Tax Assessment Act 1997 (Cth)* for excess contributions that allows individuals to make application to the Commissioner to have their excess contributions treated as if they were made in another period or disregarded if the Commissioner is satisfied that there are 'special circumstances'.
26. The Committee notes the recent successful appeal against a determination of the Commissioner under section 292-465 in the Full Court of the Federal Court of Australia in *Ward v Commissioner of Taxation [2016] FCAFC*. However, the Committee is aware of the considerable number of applications for relief against

excess contribution assessments that have been made to the Commissioner since 2007 with respect to this section and an extremely high proportion of these were rejected in most years – being in the order of 70% to 80%. On one view this relief mechanism may therefore be seen to have contributed to a significant administrative burden on taxpayers and the ATO.

27. The Committee notes the report of the Inspector-General of Taxation to the Assistant Treasurer in March 2014, *"Review into the Australian Taxation Office's compliance approach to individual taxpayers – superannuation excess contributions tax"*. The Committee is concerned that without further legislative reform this relief measure will not be adequate to address the probable significant number of excess contribution assessments that will occur following the passage of these current measures.
28. Further, the Committee considers that further work is required on the proposed amendments to section 292-465 to ensure that they appropriately capture the new kinds of capping measures – including the application of the \$1.6 million general transfer balance cap. Unfortunately in the time given for consultation the Committee has been unable to provide specific drafting suggestions, but would be pleased to give further consideration to this if it would be useful to Treasury.

Contacts

29. The Committee would welcome the opportunity to discuss its submission further and to provide additional information in respect of the comments made above. In the first instance, please contact:

- Ms Michelle Levy, Chair, Superannuation Committee (T) 02 9230 5170 (E) michelle.levy@allens.com.au; or
- Ms Heather Gray, Chair, Tax Subcommittee of the Superannuation Committee (T) 03 9603 3608 (E) heather.gray@hallandwilcox.com.au.