Friday, 26 April 2024

Retirement, Advice and Investment Division
Treasury
Langton Cres
Parkes ACT 2600

Sent via superannuation@treasury.gov.au

Dear Sir/Madam,

Re: Better Targeted Superannuation Concessions: Draft Regulations ("Draft Regulations")

Chartered Accountants Australia & New Zealand (CA ANZ), CPA Australia, Financial Advice Association of Australia (FAAA) and the Institute of Public Accountants appreciate the opportunity to respond to the Draft Regulations consultation presently underway at Treasury.

It is our overall view that these draft regulations demonstrate again that the Better Targeted Superannuation Concession (BTSC) is poorly designed and needs to be redesigned.

Our concerns with BTSC policy

Before we address the specifics of the Draft Regulations we believe it important to restate our overriding concerns with the BTSC policy:

- The consultation timeframe for this policy has been too short and should have been more open to improvements or other alternatives.
- For many taxpayers it is retrospective, especially those in defined benefit pensions.
- It treats two of the important aspects of retirement (homeownership and savings) differently from a tax perspective.
- Taxpayers who are either very good investors and/or accessed very generous contribution rules before June 2007 may be unfairly penalised.
- Taxpayers who experience investment market bubbles may also be unfairly penalised.
- Most individuals impacted are older, due to the imposition of contribution restrictions from 2007. These individuals are either subject to substantially higher drawdown requirements due to their age, or must generally release their benefits from superannuation on death. In other words, the additional tax concessions in the superannuation sector for this cohort of high balances will substantially decline over the next decade or two.
- The BTSC measures are very complex and will be costly to administer for government, superannuation funds and individuals – we consider that the cost estimates contained in

the Bill's explanatory memorandum are low: all fund members will be impacted by these policies as all administration IT systems, disclosure documents, annual statements and call centre scripts etc must be adjusted.

- It taxes unrealised capital gains which is substantially inconsistent with our tax regime.
- Investment losses (for Division 296 tax purposes) are carried forward, rather than providing an immediately refundable tax benefit to members – this creates a contingent liability for government finances.
- When account balance falls below $3 million, and does not go above it again, then tax has been paid on unrealised gains which would not be returned to the taxpayer.
- Our modelling indicates that it would be difficult to predict when tax will be payable from one year to the next. Cash flow management will be practically impossible and it will force some funds to sell assets, where they are unable to defer payment of tax. In the case of large illiquid assets, taxpayers will also be further penalised for long sale periods.
- The application of the tax for defined benefit members (as we will discuss below) is particularly complex and cannot be planned around.
- Those without a condition of release are not allowed to take money out of the system to bring their balance below the $3m threshold.
- Early stage investor incentives[1] permitted in the tax law are effectively removed.
- Applies the tax to those who die on precisely 30 June, but not other days of a financial year.
- Applies tax to those who are disabled or diagnosed with a terminal illness and received an insurance benefit from their superannuation fund that has been retained in the superannuation system.

Later we address some options to improve the existing policy or alternatives that could also be considered.

Our concerns with the Draft Regulations

The regulations ensure that for defined benefit type benefits, notional "family law" valuations are used to determine a taxpayer's proposed Division 296 tax liability.

Reference is made in the Draft Regulations to the *Family Law (Superannuation) Regulations 2001*. We note in passing that these regulations are due to sunset on 1 April 2025 and the Attorney-General's Department is currently consulting on new draft *Family Law*

[1] Australian Taxation Office (2021) *Tax incentives for early stage investors*, ato.gov.au. Available at: https://tinyurl.com/msxm8s5j (Accessed: 26 April 2024).

(Superannuation) Regulations 2025[2] ("AG Department's proposed Family Law Superannuation regulations").

Clearly before the Draft Regulations are finalised, they will need to be updated to cater for the new Family Law (Superannuation) Regulations when they are approved by the Executive Council and appropriately registered.

We also note that the AG Department's proposed Family Law Superannuation regulations will contain revised actuarial factors which are used to determine the notional actuarial value of a defined benefit pension. As part of the AG Department's consultation, it has elected not to release these revised factors stating in a related consultation paper, "It would not be appropriate to publish these methods or the factors so far in advance of their commencement as this may influence parties' behaviour in resolving disputes about family law property division. Parties may seek to either delay or expedite the process, depending on whether they will benefit from these methods or the factors in the remade Regulations which will be used to determine the family law value of relevant superannuation interests."

We also note that the *Family Law (Superannuation) Regulations 2001* currently permit the relevant Minister to approve factors specific to certain superannuation interests[3]. The AG's consultation paper says that 38 superannuation plans – including nearly all Commonwealth Government defined benefit schemes – have calculation and factors approved by the Minister.

That AG consultation paper goes onto to say that, "there is no framework for regularly reviewing approved methods and factors in the [Ministerial] Approval Instrument … most approved methods and factors were made prior to 2005, and none of these have been substantively updated since they were approved". The consultation paper expresses a preference for putting in place a process to regularly update the ministerially approved factors and calculation methods.

Conceptually we believe that notional family law valuations for defined benefit schemes will often give the most accurate value for benefits in these types of schemes.

However, given the common factors will change, and may also change for some Ministerial approved specific schemes, we cannot definitively say if the proposed valuation approach is acceptable or unacceptable.

Typically, the formulae that are used generate different values for males and females. Often the values for females will be larger because of their assumed longer life expectancy. This means two individuals, one female and the other male, in the same superannuation fund and very similar circumstances of benefit entitlements may be subject to different rates of taxation because of gender. In our view this outcome is unacceptable.

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[2] Attorney-General's Department (2024) *Exposure draft: Family law (superannuation) regulations 2024*, *ag.gov.au.* Available at: https://tinyurl.com/tsz3uvhf (Accessed: 26 April 2024).

[3] Family Law (Superannuation) (Methods and Factors for Valuing Particular Superannuation Interests) Approval 2003

We are aware that in the past the High Court has rejected an unequal treatment of taxpayers such as that described above. Although we are not constitutional law experts, we believe that this is clearly inconsistent with the principle that Commonwealth tax laws should, as far as possible, treat taxpayers of the same type in the same way.

To solve this problem, unisex factors may need to be developed. Any factors that are developed under this approach must not create discrimination compared to the factors that would be used under the government's proposed approach. We also think it would be appropriate to consider different factors for couples (given that couples typically live longer than single people).

A quick review of these approved Ministerial methods and factors shows that many of the formulae are incredibly complex. Even the standard calculation method is complex. We therefore have a reasonable expectation that only experts in defined benefits will be able to assess if a super fund has calculated the notional defined benefit value for the BTSC measure correctly. This is less than ideal and will only lead to complex inquiries for scheme administrators to answer and additional overall administration costs.

For Self Managed Superannuation Funds, it appears that the valuation of defined benefit pensions requires a judicial decision. Clearly this is inappropriate for BTSC purposes and another approach will need to be put in place.

Other changes contained in the Draft Regulations

We note the intention to update the factors contained in Schedule 1A of the *Income Tax Assessment (1997 Act) Regulations 2021*. Our reading of these changes will see the notional contributions for defined benefit schemes increase in many cases.

These higher contributions will have a flow on impact to anything that uses these contribution amounts such as contribution caps and the BTSC formulae.

Yours Sincerely,

Tony Negline

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