18 June 2021

Director
Retirement Income Policy Division
Treasury
Langton Cres
PARKES ACT 2600

Via email: superannuation@treasury.gov.au

Dear Sir/Madam

Reducing red tape for superannuation funds – ECPI measures

CPA Australia and Chartered Accountants Australia & New Zealand (the Major Accounting Bodies) welcome the opportunity to provide comments on the *Reducing red tape for superannuation funds – ECPI measures* consultation.

The Major Accounting Bodies represent over 200,000 professional accountants in Australia and New Zealand. Our members work in diverse roles across public practice, commerce, industry, government and academia throughout Australia and internationally.

The Major Accounting Bodies applaud the government for seeking to reduce red tape, and hence potentially reduce operating costs, in the superannuation regulatory environment.

Our comment focus on the following exposure draft amendments to the *Income Tax Assessment Act 1997* (ITAA97):

- Proposed change to impact of a fund having *disregarded small fund assets* (new subsection 295-387(3))
- Proposal to permit choice for trustees calculating *exempt current pension income* (new subsections 295-385(8), (9) and (10))

We note that the exposure draft states that it is intended that the above proposed changes would apply for the 2021-22 financial years and later years.

Proposed change to the impact of disregarded small fund assets

The effect of this exposure draft amendment is that it will permit impacted small superannuation funds some flexibility in how their *exempt current pension income* (ECPI) is calculated.

Presently, impacted funds will be deemed to satisfy the *disregarded small fund assets* definition in Sec 295-387 at any time in a financial year if one or more members of the fund has a *total superannuation balance* that exceeds $1.6 million, and where during for some, or all, of the income year at least one of those members was in receipt of one or more *superannuation income streams* (as defined in the ITAA97) and satisfied the *retirement phase recipient* definition (also as defined in the ITAA97). We note that the *superannuation income stream(s)* would not have to be provided by the relevant superannuation fund.

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Under the current wording of the ITAA97, when a small superannuation fund is deemed to satisfy this *disregarded small fund assets* definition the fund must use the proportionate method, as defined in Sec 295-390, to calculate the fund's ECPI. Sec 295-390 requires a trustee to obtain an actuarial certificate. Without the certificate a fund would be deemed not to have ECPI and the ordinary and statutory income of the superannuation fund would not be exempt income. This actuarial certificate requirement applies even if a small superannuation fund only has member interests that are market linked superannuation income streams in the retirement phase, such as account-based pensions.

The purpose of the exposure draft amendment is to permit small superannuation funds that satisfy the *disregarded small fund assets* definition, and that only have member interests that are *superannuation income streams* in the retirement phase, to use the *segregated current pension assets* approach, as defined in Sec 295-385 to calculate their ECPI. As a result, such funds will not need to use the proportionate method and will therefore not need to obtain an actuarial certificate.

Overall, the Major Accounting Bodies support this amendment.

At this time we do not believe that this change will create any unintended consequences.

Further Amendment Requested

We note that the existing *disregarded small fund assets* definition specifically applies for individuals that have a *total superannuation balance* of more than $1.6 million.

We further note that there is no link between the $1.6 million amount in sub-sub-paragraph 295-387(2)(c)(i) and the consumer price index increases that apply to the *general transfer balance cap*, and in turn then applies to a person's *total superannuation balance* which determines if an individual can make non-concessional contributions in a financial year.

We request that this anomaly be corrected by aligning the *disregarded small fund assets* definition with the *general transfer balance cap* definition in Sec 294-35. We also request that this change be back-dated to 1 July 2017. This will only have an impact from 1 July 2021 which is the first year the *general transfer balance cap* has been indexed since July 2017.

Proposed amendment to permit trustee choice in calculating exempt current pension income

We appreciate the intent of this measure. However, we believe it may have some unintended consequences for all superannuation funds, including those regulated by the Australian Prudential Regulation Authority (APRA).

The stated purpose of the amendment is to:

> *…choose whether to treat an asset held by the fund as a segregated current pension asset, where all of the fund's assets are held solely to discharge liabilities in relation to retirement phase interests for part of the income year, but not for whole of the income year.*

> *By choosing whether or not an asset is a segregated current pension asset, a trustee can decide whether the proportionate method or segregated method is applied to income derived from that asset when calculating [the] fund[']s exempt current pension income. It is expected that this will minimise the complexity for trustees and reduce the associated reporting costs for funds.*
>
> *In practice a trustee will only be able to exercise this choice if all of the interests in the fund are in retirement phase and all of the income derived from the fund's assets is supporting retirement phase income stream benefits payable from an allocated pension, market linked pension or an account based pension. Trustees cannot choose to treat an asset as a segregated current pension asset if amounts of income derived from the asset are supporting the payment of other superannuation benefits or are being held in unallocated reserves.*
> *(*Source pars 1.17 – 1.19 of the exposure draft explanatory materials)

We agree with this explanation of the practical impact of this amendment.

We also agree that "it is expected that this will minimise the complexity for trustees and reduce the associated reporting costs for funds", but we believe it will only be the case for a small minority of superannuation funds, where the segregated current pension assets method and proportionate method produced the same ECPI. However, for many superannuation funds it is likely that different outcomes can result from these two methods. For example, capital losses are treated differently under the two ECPI methods.

As trustees will be permitted to move into and out of both methods at multiple times throughout a year it will be necessary for trustees and their tax advisers to carefully model each available option to ensure they are maximising their beneficiaries' best interests (potentially soon to involve beneficiaries best financial interests) and are not breaching a trustee covenant.

As a result, we believe this potential change may lead to greater complexity for some funds and hence greater costs for them.

Our preference is that the government does not proceed with this suggested amendment.

Preferred ECPI amendments

In its 2018 pre-Budget submission[1], Chartered Accountants Australia & New Zealand (CA ANZ) recommended that the ECPI rules be amended to permit greater flexibility for funds with a mix of pension and accumulation money for part of the income year.

If any portion of a fund that is not 100 per cent in the pension phase (typically because there is a mix of pension and accumulation phase monies) for part of an income year, and the assets

[1] https://www.charteredaccountantsanz.com/-/media/c457ea7c033543ff97d113a662c59cac.ashx

are not segregated, the ATO believes that the SMSF trustee is required to use the proportionate method to determine the ECPI and consequentially, is required to obtain an actuarial certificate for that part of the year if it does not wish to pay income tax on fund earnings during that period.

Up to the 2016-17 financial year, it had been industry practice for funds in this situation to obtain an actuarial certificate for the *whole* of the income year. The ATO allowed this practice to be used for the 2016-17 financial year but not for future financial years.

The requirement to obtain an actuarial certificate for part of an income year is onerous and expensive for SMSFs. We do not believe this past industry practice led to revenue leakage given the method that actuaries typically employ to determine the ECPI percentage.

Consequently, CA ANZ suggested that a regulatory amendment be provided to permit industry practice to continue indefinitely.

We do not believe this issue is likely to arise in APRA-regulated funds, other than Small APRA Funds.

It is the view of the Major Accounting Bodies that this recommended amendment would provide the greatest reduction in red tape for the small fund sectors in relation to the calculation of ECPI.

If our recommended amendment was not proposed, we believe it would be better to leave section 295-385 as it is currently drafted. That is, do not amend it.

This is a complex area and we would welcome the opportunity to discuss our views with you.

For further information in relation to our submission, please contact or Tony Negline, Superannuation Leader at CA ANZ at Tony.Negline@charteredaccountantsanz.com or Richard Webb, Policy Advisor Financial Planning and Superannuation at CPA Australia at richard.webb@cpaaustralia.com.au.

Yours sincerely

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