

# Submission to Federal Government

## 2011-12 Federal Budget

3 February 2011



The Institute of  
Chartered Accountants  
in Australia



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Chartered Accountants  
in Australia**

3 February, 2011

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Dear Jan

The Institute of Chartered Accountants in Australia (the Institute) is pleased to provide you with our Budget submission for fiscal year 2011-12.

Our submission this year has been drawn together against the backdrop of a number of significant challenges confronting our national economy; looming capacity constraints, the impact of the recent natural disasters in Queensland and other states, as well as the introduction of new resource tax arrangements and the need for a long-term tax reform plan.

It is now more critical than ever that the government's budgetary decisions are developed with a sharp focus on ensuring that all major expenditure commitments are measured by principles that promote maximum value for money within the framework of suitable governance protocols.

In light of the impact of the recent floods crisis across Australia, we believe it is important for the government to reconsider whether a planned return to surplus in fiscal year 2012-13 remains necessary. The existence of a budgetary deficit position for a further one to two years could, in our view, be seen as an appropriate medium-term fiscal strategy given our overall debt levels are modest, and our expected future tax revenues are more than adequate to service the necessary borrowings.

The following submission contains the Institute's recommendations about specific changes within the tax and superannuation arena to be considered by the government as part of the process of developing the 2011-12 Budget. As one of Australia's leading independent advisers on public policy, we believe that implementation of these recommendations will go some way to strengthening Australia's taxation and superannuation systems for the benefit of the broader community.

If you would like to discuss any aspect of this submission further, please do not hesitate to contact Mr Yasser El-Ansary on 02 9290 5623 or Ms Liz Westover on 02 9290 5704.

Yours sincerely

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## About us

The Institute of Chartered Accountants in Australia (the Institute) is the professional body representing Chartered Accountants in Australia. Our reach extends to more than 67,000 of today's and tomorrow's business leaders, representing more than 55,000 Chartered Accountants and 12,000 of Australia's best accounting graduates currently enrolled in our world-class Chartered Accountants postgraduate program. Our members work in diverse roles across commerce and industry, academia, government and public practice throughout Australia and in 109 countries around the world.

We aim to lead the profession by delivering visionary leadership projects, setting the benchmark for the highest ethical, professional and educational standards, and enhancing and promoting the Chartered Accountants brand. We also represent the interests of members to government, industry, academia and the general public by engaging our membership and local and international bodies on public policy, government legislation and regulatory issues.

The Institute can leverage advantages for its members as a founding member of the Global Accounting Alliance (GAA), an international accounting coalition formed by the world's premier accounting bodies. With a membership of over 800,000, the GAA promotes quality professional services, shares information, and collaborates on international accounting issues.

Established in 1928, the Institute is constituted by Royal Charter. For further information about the Institute, visit [charteredaccountants.com.au](http://charteredaccountants.com.au)



## TAXATION POLICY MEASURES

### National tax forum in 2011

The National Tax Forum that is planned for 2011 presents an important opportunity for the federal government to create a broad-based discussion within the Australian community about the future shape of tax reform in this country.

There is, in our view, a clear appetite in the business and broader community to discuss and debate the economic analysis and recommendations contained in the report of *Future Tax System* review. Given that the recommendation for a wholesale review of our tax system emanated from the Australia 2020 Summit in 2008, and since then there has been an expectation that some form of long-term 'blueprint' for tax reform would emerge from the work completed by Dr Ken Henry and his fellow panel members during the course of 2008 and 2009.

While such a blueprint would not necessarily need to provide definitive commitments about long-term changes to the tax and transfer system, it would – at the very least – need to chart some sort of pathway for the overall direction of future reforms.

Any broad-based conversation about tax and transfer system reform will present challenges for the federal government. In our view, one of the best strategies available to effectively manage the challenges would be to ensure the conversation is kept as open as possible, so as to not artificially restrict the debate to those reforms that the current federal government has a desire or capacity to act upon.

In order for the community members to feel they have had a genuine opportunity to put forward their case for reform, they will need to feel empowered and able to raise and discuss any realistic – including politically and economically challenging – reforms they believe should be considered for the future. A good example is the widespread view of many economists and tax policy experts that Australia's Goods and Services Tax (GST) system needs to do more 'heavy lifting' from a revenue collection and 'tax mix' perspective. It goes without saying therefore that the GST regime should be an integral component of the discussion at the forthcoming national tax forum.

An unrestricted discussion at the forum is also likely to present some important logistical challenges for the government. The comprehensive nature of many tax policy issues across the tax and transfer system means that any discussion over the course of a one (or even two) day event will be limited to quite a superficial level. A large number of stakeholders representing a variety of business and social community interests will also mean that it is unlikely everyone in attendance would have an equal opportunity to put forward their case for reform in particular areas of interest to them.

In order to appropriately respond to some of the challenges outlined above, we believe it would make sense for the government to consider putting in place an architecture around which the forum can be built. A series of working groups could be established well ahead of the event. These would provide an opportunity for stakeholders to participate in detailed discussions about reform ideas within the confines of specific sub-group focus areas of the tax and transfer system. For example, sub-groups could be established around areas such as:

1. Overall tax policy vision
2. Investment and entity taxes
3. Personal tax and retirement incomes
4. Transfer system and workforce participation
5. State taxes
6. Consumption and indirect taxes.

Given the government has provided a commitment that the forum will be held sometime prior to 30 June 2011, we feel it is important that architecture around the forthcoming discussion should be outlined well in advance of the May Budget announcement, to allow sufficient time for working groups to convene and commence preparatory activities.



### **Proposed new flood levy**

The recent flood relief package announced by the government in response to the catastrophic natural disasters in Queensland and other states is seen by the Institute as critically important to the commencement of the rebuilding phase for affected people and communities.

While there is no doubt significant infrastructure expenditure is likely to be incurred by the federal government, we question the inclusion of a proposed new flood levy as part of the response package. In our view, it would have been preferable for the government to avoid the introduction of a new tax – however modest it may be at low to middle income levels – and instead fund the increased costs out of consolidated revenues boosted by cuts to under-performing expenditure programs.

Furthermore, a delayed return to budget surplus, beyond 2012-13, is regarded by the Institute as being a prudent fiscal management strategy in the context of the significant financial and economic impact of the recent flood crisis.

If the proposed flood levy is introduced with effect from July 2011, it will be critically important, in our view, for the new funding generated under the levy to be clearly isolated [in budgetary terms] from consolidated tax revenues. While this would carry some considerable costs to the government in respect of administration, we believe it is an important initiative which would establish transparency in respect of the extent of revenues generated via the new impost.

The introduction of specific governance arrangements around the collection of the proposed flood levy revenues must also be accompanied by similar arrangements in relation to the infrastructure expenditure commitments that the funds are ultimately directed towards.

We believe the government (working in conjunction with the relevant state governments) should establish an agreed set of principles against which each proposed infrastructure project is assessed, prior to a funding allocation commitment being provided. These principles should be developed in close collaboration with representatives of the local communities impacted by the floods, while drawing on the expertise of the broader business community in undertaking 'competitive prioritisation' and 'cost-benefit' assessments of major funding commitments. Processes such as these will help deliver an important sense of transparency and public accountability in respect of the revenues collected through the imposition of the new flood levy on taxpayers.

While the recent flood crisis was an unexpected natural disaster on a massive scale, it was not unpredictable. Australia's climate often results in natural disasters that have a direct impact on a wide portion of the populace. It is for this reason that we believe the government should consider how best to ensure adequate natural disaster relief funding on an on-going basis, to reduce the need for special one-off and temporary levies to be imposed on taxpayers to meet short-term funding shortfalls. It would be preferable for on-going subsidy of such a fund to be met from consolidated revenues, consistent with other funds established to cover other known future costs.

### **Special investment allowance for businesses impacted by recent flood crisis**

It is widely anticipated that many of the businesses directly impacted by the recent flood crisis are likely to face significant financial pressures in meeting reconstruction and refitting costs in order to recommence full capacity trading and business activities.

It may therefore be appropriate for the government to consider the introduction of a targeted investment allowance for impacted businesses, to provide additional assistance and incentives to purchase new plant and equipment in replacement of lost or damaged equipment.

The temporary investment allowance that was introduced in Australia in 2009 during the global economic downturn could be adapted for the purposes of this initiative.



## Proposed new resource tax arrangements

As Treasury will be aware, the Policy Transition Group (PTG) has recently delivered its final report in respect of the proposed new resource tax arrangements originally announced by the government in May 2010.

It is our understanding that the recommendations put forward by the PTG are currently being considered by the government. Once that process has been worked through, it is our recommendation that the government release a White Paper outlining its preferred policy position on certain design aspects of the new tax arrangements, rather than reaching a final policy position at this point.

The benefit of the White Paper approach is that it would allow a further period of consultation and debate in relation to the proposed design of the new minerals resource rent tax, given the significant impact the new tax arrangements will have on the Australian mining sector.

Ultimately, we believe that a further round of consultation around the detailed design parameters would likely deliver a much more cohesive tax regime that is less susceptible to major design flaws being uncovered once the tax arrangements come into existence from July 2012.

Consistent with recommendations put forward by the Institute in its submission to the PTG entitled '*Digging In and Drilling Down*', we believe that resolution of the questions surrounding the extent of crediting of state-based royalty payments must be prioritised above all other issues. Given the significant financial burden that could arise for impacted companies in the resources sector from the existence of dual tax regimes (being the new minerals resource rent tax existing alongside continuing payments to state governments for royalties), it is critically important that the federal government initiate a dialogue with all states and territories through the Council of Australian Governments Forum to:

1. Initially, move towards the full crediting of all royalty payments; and
2. In the medium-term, reach agreement on a timetable for eventual abolition of state-based mining royalty payments.

The eventual abolition of state-based mining royalty payments is consistent with the recommendations in this area contained in the *Future Tax System* report.

## Reforms to the foreign source income attribution rules

The Institute has been extensively involved in Treasury's consultation processes in relation to the reform of the controlled foreign company (CFC) rules, as well as other improvements to the foreign source income anti-tax deferral rules announced in the 2009-10 Federal Budget. The Institute has been a long-time advocate of changes to these provisions, consistent with the recommendations of the Board of Taxation in its September 2008 report.

### *Controlled foreign company reforms*

In our view, the proposed CFC reforms are the cornerstone of the government's reform objectives in the international tax policy arena. It is our understanding that reforms to these rules are still being worked through by Treasury and the government, and that exposure draft legislation is expected in the near future. Taxpayers across a number of industry sectors are eagerly awaiting these changes, which are expected to deliver a modernised attribution regime that reduces complexity and compliance costs and boosts the competitiveness of Australian businesses with offshore operations.

The Institute encourages the government to move towards finalisation of these reforms as quickly as possible, so that legislation can be introduced into Parliament in the first half of 2011 for an effective commencement date of 1 July 2011. It may also be appropriate to consider allowing taxpayers the option of applying the new laws from 1 July 2010, in recognition of the lengthy period of time that has elapsed since the government's initial announcement in May 2009.



### *Anti-roll-up fund rule*

The Institute supported the repeal of the foreign investment fund (FIF) rules effective from the 2010-11 income year, as announced by the government in the 2009-10 Federal Budget. At the time of the announcement, it was indicated that the FIF rules would be replaced with a specific and narrowly-defined anti-avoidance rule known as the 'anti-roll-up fund' rule.

Despite exposure draft legislation having been released for consultation in April 2010, no legislation has yet been introduced into Parliament to enact the measures since that time. Given that the anti-roll-up rule will presumably operate from the 2010-11 income year, the Institute urges the government to expedite introduction and passage of enacting legislation so that taxpayers have certainty as to the final form of the new rules.

### **Tax issues relating to private equity investment**

Treasury and the government will be aware of the uncertainty that persists in relation to Australian-based investments of foreign private equity firms. While the Australian Taxation Office (ATO) has taken steps in the last few months to provide some clarity around its interpretation of how the relevant tax laws apply to leveraged buyout investments, the underlying policy of the federal government remains unclear. We believe this issue needs urgent consideration as part of the 2011-12 Budget.

It is our understanding that prior to the calling of the August 2010 federal election, a discussion paper was prepared for release by Treasury which posed a number of policy questions around how Australia's taxation laws should apply to leveraged buyout investments. A discussion paper that canvassed issues relating to these types of transactions, the benefits they deliver to the national economy, and the appropriate government policy that should be reflected through our taxation laws should be released for discussion and debate as soon as possible.

A robust national discussion about the underlying tax policy in this area would go some way to restoring confidence in Australia as an attractive place in which to invest and do business, consistent with the principles of the November 2009 Australian Financial Centre Forum report, *Building on our Strengths*.

### **Review into certain aspects of the taxation of trusts**

The Institute has been a long-time supporter of the need to update the trust income tax provisions in Division 6 of the Income Tax Assessment Act 1936 (ITAA 1936) with a view to re-writing the provisions into the Income Tax Assessment Act 1997 (ITAA 1997). It is for this reason that the Institute has endorsed the government's recent announcement about the commencement of a new project in this area during 2011.

It is our understanding that this project will commence with an initial consultation paper to be released by Treasury in the first part of 2011 which, importantly, draws on the expertise of the Tax Design Review Panel and the Board of Taxation.

As part of this process we believe the opportunity should be taken to update and re-write related provisions, such as the trust loss rules contained in Schedule F of the ITAA 1936. It is worth pointing out that the Institute has previously made a number of specific recommendations in relation to the current operation of Schedule F, including most recently in its [2010-11 Budget submission](#).

Given the number of Australian businesses that operate through commonplace trust structures, the Institute urges the government to allocate appropriate resources to this project to ensure it is completed in a timely fashion and produces effective outcomes.

The Institute also welcomes the fact that the government has recognised that certain amendments cannot wait for completion of the broader project. We therefore support the introduction of these amendments into Parliament before 30 June 2011.



These proposed amendments to the averaging and farm management deposit provisions aimed at farmers should ensure that they are insulated from the consequences of the High Court's recent decision in *Commissioner of Taxation v Bamford* for the 2011 income year, with affected farmers continuing to rely on Taxation Ruling TR 95/29 in respect of the 2009-10 and earlier income years (albeit that, strictly speaking, the ruling only applies to the averaging provisions).

At the time of preparing this submission, the Board's advice on other amendments which require 'fast tracking', and the government's response thereto, were not available. However, the Institute is of the view that urgent amendments should be made to codify the ability of trusts to stream franking credits and capital gains both retrospectively and prospectively.

The Institute is of course willing and prepared to assist Treasury, the Board of Taxation and the government with any aspect of their work on this critically important project during 2011 and beyond.

### **Dedicated tax regime for managed investment trusts**

Legislation to put in place a dedicated tax regime for managed investment trusts (MITs), which incorporates the bulk of the recommendations made by the Board of Taxation in its report on the tax arrangements applying to MITs, is expected to be introduced from 1 July 2011.

At the time of writing, Treasury was reviewing submissions made in relation to its October 2010 discussion paper on the design and implementation details of the reforms, with a further round of consultation on exposure draft legislation foreshadowed for the first half of 2011.

The Institute supports the introduction of a new tax system to provide certainty for managers of, and investors in, MITs without added complexity or compliance costs. In our response to Treasury's discussion paper, we raised a number of issues, to ensure this objective can be achieved by the majority of funds which are intended to fall within the scope of the new rules.

Finally, given the time pressures associated with finalising draft legislation and introducing and passing these new laws prior to 1 July 2011, if industry believes that such a delay is necessary, it may be appropriate to consider a one year delay to the proposed commencement date. The Institute would support a commencement date of 1 July 2012.

### **Wholesale review of Division 7A**

We believe the government should consider asking the Board of Taxation to commence a major overhaul of the current Division 7A tax laws.

There have been a number of concerns raised by taxpayers and the ATO in relation to the operation of Division 7A over the last few years. These concerns have often resulted in an 'ad-hoc' and piecemeal approach to fixing such issues. Based on our analysis, legislative changes to the operation of Division 7A have been made in each of the 1998, 2002, 2004, 2005, 2007 and 2010 income years. These changes have resulted in overly complex laws and a diminished ability of taxpayers to effectively comply with their obligations under these laws.

In our view, the recent legislative and administrative developments in 2009 and 2010 have increased the complexity of Division 7A, making it difficult for both tax practitioners and taxpayers to work with the intricate interactions between the new legislative provisions and certain ATO rulings and determinations.

The Institute believes a major review and re-write of Division 7A into ITAA 1997 would result in a more consistent application of underlying policy throughout the provisions, and would significantly simplify the current structure of the laws. In our view, it would also be reasonable to assume that such a project would greatly enhance the understanding of the laws and thereby improve taxpayer compliance in this area.



### **Transferring remaining provisions of the ITAA 1936 to the ITAA 1997**

During the recent federal election campaign, the government announced its commitment to a principles-based approach to tax design which aims to deliver a simple, transparent, responsive, accountable and accessible tax system. Part of that announcement also encompassed a recommitment towards transferring the remaining provisions in the ITAA 1936 to the ITAA 1997, to deliver a single, modern set of income tax laws.

The Institute supports this commitment by the government and encourages Treasury to take all necessary steps required to bring about these changes in the next few years.

### **Application of GST laws to financial services transactions**

The Institute has consistently argued that Australia's regime of input taxation of financial services is inefficient, internationally uncompetitive and places the country at a significant disadvantage compared with its competitors in regional financial services centres. The recent economic analysis completed in the *Future Tax System* report confirms the Institute's view on this point.

Consistent with the Institute's submission, the *Future Tax System* report recommended that the government should "[r]eplace the current inefficient input taxation of financial services under the GST with a more efficient financial services tax..." to ensure that the consumption of financial services by Australian households is fully taxed, and their consumption by businesses is relieved from tax like any other business input.

In our view, it would be appropriate for the government to carefully consider the recommendations made in this area, with a view to amending the underlying policy to deliver the following outcomes for financial services:

- Fully tax activities under either the existing GST, or a separate financial services tax; and
- GST-free classification for business-to-business transactions.

### **GST treatment of government subsidy payments**

In the *TT-Line Company Pty Ltd v Commissioner of Taxation* [2009] FCAFC 178 case in 2010, the Full Federal Court held that the GST law is capable of giving rise to non-recoverable GST amounts on government outlays in cases where an agency subsidises the price paid by consumers for goods and services. Many believe that the interpretation adopted by the Court is in direct contradiction to the underlying policy objective in this area of the GST law, and demonstrates that the policy of taxing final private consumption is not being achieved in the area of government subsidies.

The Institute recommends that the GST law be amended to ensure that:

- Government expenditure does not include non-recoverable GST costs, i.e. input tax credits are allowed; and
- Government-to-government payments are either out of scope or GST-free.

This proposal is consistent with the recommendations of the *Future Tax System* report to improve the efficiency and reduce the compliance costs of the GST law in this area.

### **Valuation of non-cash fringe benefits**

Winding back the foreign earnings exemption under section 23AG of the ITAA 1936, and the application of the ATO's recent interpretation outlined in TD 2011/1, means that many non-resident employers fall outside the Pay-As-You-Go (PAYG) system and therefore the fringe benefits tax regime as well.



As a consequence, many employees who work overseas (but remain tax residents of Australia) will become subject to income tax on benefits received under section 15-2 of the ITAA 1997. However, the tax laws in this area do not contain any valuation rules for such non-cash benefits.

This leads, at best, to a multitude of compliance difficulties, as affected employees will not know how to value taxable fringe benefits. At worst, there are some serious inconsistencies with benefit valuation rules in the Fringe Benefits Tax (FBT) laws, which provides for many exemptions and concessions that cannot be utilised under income tax rules. This will create particular problems for employees working overseas and receiving benefits such as Living Away From Home Allowance, which would be largely exempt under the FBT law, but could be fully taxable under income tax. Other benefits, such as motor vehicles and benefits whose value can be reduced under the 'otherwise deductible rule' will also be potentially more harshly taxed under income tax treatment.

As a result, we believe the government should take steps to provide clarity around the valuation rules for taxable non-cash benefits. A potentially simple and attractive solution would be to mirror the FBT rules, in order to ensure consistency of valuation and to ensure affected employees are not unfairly taxed by virtue of the vagaries and inconsistencies of the application of the PAYG and FBT laws to Australians working overseas.

As an alternative, the government could consider a reinstatement of the previous section 23AG exemption as it stood prior to 1 July 2009.

### **Tax deductibility of financial advisory services**

The Institute believes all Australians should have access to consistent, affordable financial and tax advice from their choice of appropriately qualified and experienced professional advisers across the financial services industry.

The Institute is currently participating in consultation forums on the government's *Future of Financial Advice* (FoFA) reforms around the provision of financial advisory services in Australia. Part of the reform package includes expanding the availability of low-cost, 'simple advice' to improve access to, and affordability of, financial advice.

In alignment with these reforms, the Institute believes the government should address tax deductibility of financial advice in the upcoming Budget. A review of the tax deductibility of financial advice fees would support the FoFA reforms aimed at improving accessibility and affordability of financial advice.

The determination issued by the ATO dealing with the deductibility of investment advice is TD95/60. The ruling stipulates that fees charged for drawing up an investment plan are not deductible, because they constitute expenditure of a capital nature incurred while putting the income earning investments in place. However, ongoing management fees or retainers are generally deductible, because they are expenses incurred in the management of income producing investments. We believe it is an anomaly that the ongoing management of superannuation, for example, is not tax deductible (as superannuation is not income producing), but where the advice on superannuation is related to taxation, this advice is tax deductible.

The Institute recommends changes to the legislation to allow tax deductibility for fees relating to the development of a financial plan. The Institute also recommends the widening of the ongoing management tax deductibility to include non-income-producing investments (eg superannuation) and other non income-producing strategic financial planning (eg insurance). Allowing tax deductibility would appear to be consistent with the government's objectives of making financial advice more accessible and affordable to Australian taxpayers.



## Research and Development ('R&D') tax credit

The Institute supports a delayed commencement date to the proposed new R&D regime. If the Bill giving effect to these reforms is passed through Parliament during July 2011, a commencement date of 1 July 2011 would be appropriate. If however the Bill does not pass through Parliament until after July 2011, then our preference would be for the commencement date to be delayed to 1 July 2012. This approach provides taxpayers with a reasonable timeframe within which they can make business decisions in respect of long-term investment in R&D activities.

## Carbon pricing mechanism

The Institute believes the government should introduce a price on carbon, as we believe that an explicit carbon price signal is a necessary part of the policy response to climate change – one that will create certainty for the market and catalyse the transition to a low-carbon economy.

We believe that the majority of revenue collected from the carbon price mechanism should be earmarked for reinvestment in programs relating to climate change action, including renewable energy, low emissions transportation, energy efficiency incentives, and subsidies to offset cost increases for low income earners.

The Institute also encourages the government to utilise complementary broad-based tax measures such as the R&D tax incentive to deliver enhanced tax benefits for innovations in the key area of low-carbon infrastructure / assets, such as renewable energy and zero-emissions technologies.

Equally, tax concessions that promote environmentally undesirable behaviours should be reviewed, such as the Fringe Benefits Tax concessional statutory rate for motor vehicles, and other subsidies and concessions such as the various fuel schemes that currently exist.

## Funding of government agencies, various statutory offices and other major initiatives

### *Proposed new Tax System Advisory Board*

The recent announcement by the government to consult on the establishment of a Tax System Advisory Board to advise the Commissioner of Taxation and the ATO's Executive Committee on the general management and organisation of the ATO is a positive initiative in further enhancing the integrity and standard of Australia's taxation system.

The panel appointed to facilitate consultation on the proposal is due to report back to the government by the middle of this calendar year. The Institute anticipates therefore that the new Board could be established during the 2011-12 financial year.

An important aspect of establishing the proposed Board will be ensuring that an appropriate level of funding is allocated to attracting the type of experienced business professionals proposed by the government.

### *Board of Taxation*

In another key improvement to the governance of the tax system, the government announced in August 2010 that the Board of Taxation will, in consultation with the government, be able to initiate its own reviews to examine how current tax policies and laws are operating.

The Institute anticipates that increased funding will be required for the Board of Taxation's expanded role; for instance, to engage in consultation with various stakeholders proposing reviews and undertaking preliminary scoping and analysis.



### *Inspector-General of Taxation*

The Inspector-General of Taxation (IGT) plays a pivotal role in the oversight of the ATO as administrator of Australia's taxation system. Established in 2003, the IGT Office has so far undertaken numerous crucial reviews into the ATO's practices and identified major process and system improvements for the benefit of taxpayers, including businesses, not-for-profits and individuals.

The Institute understands that funding for the IGT Office has not been reviewed since its inception in 2003. Armed with a relatively small workforce of only seven people, the IGT office has front-line responsibility, along with a range of other statutory bodies and government agencies, for overseeing an ATO workforce of more than 24,000.

It would seem appropriate for the government to consider increasing the level of funding for the IGT office, in recognition of both the valuable role it plays in Australia's tax administration, and the growing pressures and demands being placed on the IGT's limited resources.

It may also be appropriate for the government to consider providing the ATO with additional funding to establish a sub-group within the organisation, charged with coordinating the implementation of IGT recommendations identified in reports prepared for the government. A group dedicated to this purpose would help ensure full transparency around the implementation of process improvement initiatives in a coordinated and systemic manner.

### *Tax agent services regime*

As the government will be aware, the new regime for the regulation of all Australian tax and business activity statement (BAS) agents commenced in March 2010.

Many of the Institute's members believe the new regime has not been adequately publicised within the Australian taxpayer community. Given the new regime implements a range of new protections for consumers of tax and BAS agent services, and given that a very high proportion of taxpayers (more than 73%) use the services of a tax agent every year, it would seem appropriate for the government, in conjunction with the Tax Practitioners Board, to consider allocating funding for a roll-out of a national awareness campaign explaining the benefits of the new regulations to consumers of tax and BAS agent services.

### *Department of the Treasury*

Given the forthcoming national tax forum will occur in the first half of 2011, it would seem appropriate for the government to allocate additional funding to Treasury in order to cater for additional specialist economic, tax and public policy resources required to carry out work on the design and implementation of any reforms stemming from the forum.

The Institute is aware that Treasury's Revenue Group resources have been stretched and running at full capacity for some time in managing the or routine tax policy issues that emerge from day-to-day activities.

Treasury's capacity to take on major one-off and long-term projects will, in our view, impose a significant burden on top of that which already exists. It would be problematic to re-deploy tax policy resources from other parts of Treasury's Revenue Group because that is likely to cause significant disruption to the ongoing and important activities of the Group.

We believe that on an increasing basis, Treasury will also need to have access to specialist accounting resources in order to assist with the design and development of taxation laws that are more closely aligned with International Financial Reporting Standards. It may therefore be appropriate for the government to consider providing additional funding for Treasury in order to establish a small team within the department to achieve a closer alignment between tax laws and accounting standards wherever possible.



## **SUPERANNUATION POLICY MEASURES**

### **Concessional Superannuation Contribution Caps**

The government should consider changes to the way the concessional superannuation contributions cap system operates and introduce a carry forward provision for these contributions, rather than an annual “use it or lose it” limit.

A carry forward provision will enable many Australians to make additional contributions when they are most able to do so. Typically, most Australians will never be able to contribute the maximum allowable contribution at times in their lives when, for example, they are raising families or paying mortgages. The system needs to have the flexibility to accommodate increased superannuation contributions at later stages of life when incomes are higher and expenses are diminishing. This would allow Australians to catch up on superannuation contributions to compensate for earlier years when they were not able to make maximum contributions. Current measures allowing for increased caps for those over the age of 50 are too little, too late, for many Australians.

Irrespective of the way the system operates, the current cap for concessional superannuation contributions is too low to enable Australians to adequately save for their retirement.

Australia’s population is ageing and around 80% of Australians aged over 65 will soon depend on some form of aged pension. It is therefore critically important to encourage Australians to be self-reliant in retirement. The current caps are not consistent with achieving this objective.

The Institute believes that when budgetary pressures ease, the government should re-consider the level at which the concessional contributions caps are set and reinstate the original caps to \$50,000 for those under 50 years of age and \$100,000 for those aged over 50. At that time, a review of the government’s 2010-11 Budget announcement to limit the higher amount for over 50’s to those people with superannuation account balances less than \$500,000 will need to be reconsidered. This review would examine whether the low balance criteria is warranted and, if it is, that it is set at the appropriate level.

### **Excess Contributions Tax (ECT)**

The Institute acknowledges that the policy intent of superannuation contribution caps is to limit the amount of superannuation contributions for individuals, to encourage consistent saving for retirement over a person’s working life and to limit access to concessional taxation (albeit that we do not believe that the caps are set at the appropriate level).

We believe, however, that the penalty for making contributions beyond the contributions caps is excessive, unwarranted and inconsistent not only with the policy objective, but with penalties for breaches in other areas of tax law. Changes are required to ensure that a fairer system is in place and will remain consistent with the government’s policy objective to encourage saving for retirement.

Where excess contributions have been made, fund members should be given the option of either:

- Paying ECT – this may be an easier option for higher income earners where they would otherwise have made non-concessional contributions (having already paid the same amount of personal income tax); and
- Opting to have excess contributions refunded out of the superannuation system. Any earnings accumulated on excess contributions should also be refunded (ascertained by way of actuarial certificate). Amounts refunded and earnings would need to be included in personal income tax returns.

The legislation needs to be amended to accommodate a number of scenarios in which inadvertent breaches of the contribution caps have occurred and deal with them in a fair and reasonable manner.



Despite the inclusion of clauses which give the Commissioner of Taxation some discretion to disregard or re-allocate contributions to other years in special circumstances, the Institute does not believe this discretion is broad enough to address many of the inadvertent breaches that have occurred.

Further consultation with industry professionals on the implications and impact of ECT would be appropriate. The Institute recommends that the government consider the following changes to the current laws in this area:

- Introduce one cap for both concessional and non-concessional contributions, with a maximum concessional amount, to eliminate the problem for taxpayers who, at financial year end, do not have sufficient, anticipated income to claim the full amount of superannuation contributions or do not qualify to claim a deduction;
- Provide taxpayers the option of paying the ECT or have their superannuation fund refund contributions in excess of the contributions caps;
- Impose a less severe penalty for excess contributions, that will encourage members not to become complacent around their superannuation contributions; and
- Expand the Commissioner of Taxation's discretionary powers to disregard or re-allocate contributions to enable fair treatment of honest mistakes that have occurred to date.

### **10% rule - Deductibility of personal superannuation contributions**

The Institute believes that in the interests of equity, a tax deduction for personal superannuation contributions should be made available for those employees who receive employer superannuation support.

The current "10% rule" means that only taxpayers who earn less than 10% of their assessable income from an employer source can claim a tax deduction for personal superannuation contributions. Access to this deduction is actually only available to relatively few people.

Employees who work for employers that allow them to salary sacrifice additional superannuation contributions effectively overcome this issue. That is, they can forgo salary and wages to contribute (or have contributed for them), tax effective superannuation contributions up to the concessional cap.

Conversely, employees whose employers do not allow them to salary sacrifice are disadvantaged. Australians trying to save for their retirement should not be deprived of superannuation concessions by working for an employer who does not allow them to salary sacrifice into superannuation. The Institute considers that it would be more equitable and efficient to permit employees to make personal concessional contributions in order to "top up" their employer contributions.

We consider that this policy would encourage people of all ages and wage levels to provide more for their retirement, including employees who do not salary sacrifice additional amounts because their employer uses these contributions to satisfy their 9% superannuation guarantee obligations (see below).

This policy would also ease the administrative burden on small businesses, as they would no longer be compelled to offer their employees salary sacrifice arrangements.

### **Salary Sacrificing and Superannuation Guarantee Contributions**

Under current legislation, employers who offer employees salary sacrifice arrangements to increase their superannuation contributions are able to use the salary sacrificed amounts to satisfy their 9% superannuation guarantee obligations. This discourages employees from making additional contributions to increase their retirement savings, because by doing so they may be forgoing their entitlement to 9% employer super payments. While many employers will pay the 9% superannuation guarantee regardless, some will take advantage of the legislation for their own gain.



A further anomaly exists in the legislation affecting employees with salary sacrifice arrangements. Currently, employers are only obliged to make superannuation guarantee contributions based on their employees' reduced wage amount. That is, the superannuation guarantee amount is calculated on salary and wages after salary sacrifice.

Both of the above issues are at odds with the government's policy of requiring 9% of earnings to be contributed to superannuation. In effect, current legislation reduces the amount an individual saves over their working life, and instead benefits the employer.

Addressing these two issues should have minimal impact on the budget bottom line, while rectifying inequities and directing monies to their rightful place in superannuation.

The Institute recommends that the government amend the Superannuation Guarantee (Administration) Act 1992 so that:

- Employers are not able to utilise salary sacrificed superannuation contributions to satisfy their superannuation guarantee obligations; and
- Employers are required to calculate their superannuation guarantee obligations on a gross basis, before salary sacrifice arrangements are considered.

### **Timing of employer superannuation contributions**

Employers making superannuation guarantee contributions are obliged to make these contributions within 28 days after the end of the quarter. The government may wish to consider requiring these contributions to be made more frequently to ensure contributions are submitted to superannuation funds in a more timely fashion to benefit employees.

Furthermore, there is currently no legal requirement for the timing of employer contributions that are made as a result of an employee's salary sacrifice arrangements, other than what may be prescribed under an award or salary sacrifice agreement. The Institute would support a requirement for employers to make salary sacrificed contributions, at a minimum, in line with superannuation guarantee contributions. Consideration could also be given to ensuring such contributions are made as part of an employer's normal payroll cycle.

### **\$450 per month threshold for superannuation guarantee contributions**

Employers are currently not obliged to make 9% superannuation guarantee contributions for employees who earn less than \$450 per month. It has been advocated by sectors of the superannuation industry that this threshold for superannuation contributions should be removed to, in part, fill the gap in superannuation savings for low income earners.

The Institute believes the \$450 per month threshold is appropriate. If the threshold is removed, the increased burden on businesses will far outweigh the benefits of minimal superannuation contributions for workers in this income group. Removing the threshold may act as a disincentive for businesses to employ part time/casual workers due the increased costs in employment and administrative burden. Furthermore, the costs associated with making such minimal contributions may be absorbed by limited or no future wage increases. These particular workers are far more likely to benefit from increased cash-in-hand rather than minimal superannuation contributions.

We also note that until the government's announcement in the 2010-11 budget regarding the super contributions tax rebate for low income earners becomes law, superannuation contributions below the threshold will be subject to superannuation contributions tax. Income of \$450 per month will not incur income tax. Therefore, the potential for a detrimental outcome for taxpayers exists should the threshold be removed at this time.



### Superannuation Death Benefits

Because of the interaction of the death benefit and terminal illness payment rules there are some death benefit beneficiaries who will be liable to pay tax upon the receipt of those benefits. Tax on death benefits may apply where the deceased:

- Was not in a married or de facto relationship;
- Had non-dependent children or other beneficiaries;
- Died suddenly; and
- Had a taxable benefit in excess of the low tax threshold.

In order to pay this tax, superannuation funds are required to maintain the taxable / tax free percentage for the life of the member, although this is not relevant to the member's tax affairs after the age of 60. As this information is not gathered by a government agency, there is a risk that the information will not be retained accurately and that the tax will not be collected equitably.

The Institute recommends that the government consider making changes to the ITAA 1997 to provide that all death benefits from taxed funds should be treated as tax-free; that is, as if they were paid to a dependant. This would give the same tax result as if, prior to their death, the deceased had removed all their benefits from superannuation and bequeathed the amount to their beneficiaries as part of their estate.

