

SUPERANNUATION UPDATE

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In this month's Update ...

We are only a few months into 2006, and it already looks like another interesting year for superannuation!

In this, our first Superannuation Update for 2006, we ask ourselves what sort of a year will this be for superannuation members and advisors? The principal recent developments are outlined and discussed in this Update.

Please contact Arthur Athanasiou or James Shattock if you need assistance or more information about these developments or any other superannuation matter—their contact details are shown below.



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Superannuation holding accounts to close after 30 June 2006

The superannuation holding accounts ("SHA") (previously known as the superannuation holding accounts reserve) is a special account administered by the Australian Taxation Office. A small number of employers use the SHA special account to meet their superannuation guarantee obligations for their employees.

The SHA special account is not a trust fund or an alternative superannuation fund. It is a holding mechanism designed to protect employee's small superannuation amounts until they can be transferred into a complying superannuation fund or retirement savings account.

The SHA special account will be closed to employer deposits after 30 June 2006. Therefore, until 30 June 2006, payments to the SHA special account can satisfy a contributing employer's superannuation guarantee obligations, and a SHA special account

can be used as an employer fund for the 2006 financial year, provided the payment is made before 1 July 2006. However, after 30 June 2006, the SHA special account will be closed to employer deposits. From that time, an employer will not be allowed to make a deposit into the SHA special account for its employees to satisfy the employer's superannuation guarantee or choice of superannuation fund obligations.

If an employer is currently using the SHA special account, it will need to make alternative arrangements with a complying superannuation fund or retirement savings account to meet superannuation guarantee and choice of superannuation fund obligations. Employers are encouraged to make these arrangements before 30 June 2006 to avoid paying the superannuation guarantee charge.

Submission on splitting and merging superannuation funds

On 30 January 2006, the Taxation Institute of Australia ("TIA") lodged a submission with the Minister for Revenue and Assistant Treasurer relating to the splitting and merging of superannuation funds, in particular self-managed superannuation funds ("SMSFs"). The TIA is concerned that there is no exemption in the capital gains tax ("CGT") provisions for the "splitting" of trusts and in particular for the splitting and merging of superannuation funds.

As stated in the TIA submission, in most cases, the purpose for seeking to split an SMSF is for practical exigencies, for instance, separation of spouses, family members or former business partners. This submission makes the point that without clear exemption or roll-over relief, separated spouses and business partners are effectively required to remain in an SMSF with former partners.

The TIA submission also notes that when two single people join together as a couple, they may have two

SMSFs and there can be significant savings in merging the two funds into the "family" fund.

The TIA contends in its submission that the lack of clear CGT relief on the transfer of assets between superannuation funds (on both the splitting of funds and their consolidation) is both extremely inflexible and inefficient, and leads to the creation of an unnecessary number of SMSFs.

The key elements of the proposed superannuation fund roll-over relief as outlined in the TIA's written submission include (among other things) that the roll-over apply to the transfer of CGT assets from an existing superannuation fund to another superannuation fund provided that interests of specific members were substantially the same, with the new fund taking over the same CGT cost base as the original fund.

We will advise in due course as to the outcome of the TIA's submission.

Anti-Money Laundering and Counter-Terrorism Financing Bill 2005

The above Bill ("the AML/CTF Bill") is not yet finalised and it will probably be referred again to the Senate committee. If this Bill is to become law, then it may impact on superannuation funds, including SMSFs.

At this stage, it appears that the central thrust of the AML/CTF Bill is to require entities undertaking certain

activities to identify the person they are dealing with, and, where necessary, report certain persons and their activities to the regulator.

The AML/CMT Bill lists the types of activities that are considered vulnerable to money laundering or terrorism financing. These services are called "designated services". These services include

Anti-Money Laundering and Counter-Terrorism Financing Bill 2005 *cont*

payment of a pension, accepting a contribution, roll-over or transfer in respect of a new or existing member, and also cashing, rolling over or transferring an interest held by a member of a superannuation fund.

An entity that provides a designated service is considered to be a "reporting entity". Therefore, under the AML/CTF Bill, a trustee of a superannuation fund, including an SMSF, would be a "reporting entity".

The AML/CTF Bill imposes various obligations on reporting entities, including the following:

- to verify a customer's (that is, a member's) identity before providing the designated service (for instance, paying a benefit or receiving a contribution). However, the AML/CTF Bill may exempt superannuation trustees from "up front" identification;
- to give the regulatory authority (being the Australian Transaction Reports and Analysis Centre ("Austrac")) reports of suspicious activities (including where the trustee has reasonable grounds to suspect that (a) information it holds about the provision of a service may be relevant to the investigation of tax evasion or other offence, or (b) the provision of the service is preparatory to the commission of a financing of terrorism offence);

- to report to Austrac if they provide a service that involves a threshold transaction, which includes the transfer of more than \$10,000. Without amendment, this reporting requirement means that trustees of funds must report every transfer, roll-over or benefit payment of \$10,000 or more to Austrac within 10 days of performing the transaction; and
- to develop, maintain and comply with AML/CMT programs, designed to ensure that a reporting entity takes appropriate action to identify and materially mitigate the risk that the provision of a designated service might facilitate a transaction that is connected with the commission of a money laundering or financing of terrorism offence.

It is submitted that if the AML/CTF Bill is to become law without further amendment, then it may impose unreasonable and inappropriate obligations on trustees of superannuation funds, especially SMSFs.

Recent Interpretative Decisions and Determinations

There have been several interpretative decisions ("IDs") and determinations in the last two months in relation to superannuation that should be considered. These include in particular the following.

ATO ID 2006/19 – superannuation deductions and the research and development tax concession

In this ID, the issue was whether an eligible company could claim a tax deduction under subsection 73B(14) of the *Income Tax Assessment Act 1936* ("ITAA 1936") for superannuation contributions paid in respect of an employee that is engaged in research and development activities.

The company was an eligible company which carried out "research and development activities" as defined in ITAA 1936 in Australia on its own behalf.

The company was registered under the *Industry Research and Development Act 1986* for that income year with the Industry Research and Development Board in respect of those activities, and the company's aggregate research and development amount is greater than \$20,000 in the income year.

The company made contributions to a superannuation fund by way of benefits for an "eligible employee", as defined in ITAA 1936. This employee is directly engaged in research and development activities for the whole of the income year.

In this case, it was decided that the company could claim a deduction at a concessional rate, for superannuation contributions for an employee, under s 73B(14) of ITAA 1936, to the extent that the employee is engaged in research and development activities of the company.

This decision was based on the fact that a deduction is available under s 73(B)(14) of ITAA 1936 if an eligible registered company incurs relevant research and development expenditure (other than contracted expenditure) and has an aggregate research and development amount greater than \$20,000 in the income year. The deduction is available at a rate of 125% of the expenditure incurred.

Recent Interpretative Decisions and Determinations *cont*

The term “research and development expenditure” is defined in ITAA 1936 to include “salary expenditure”, which in turn includes the portion of “contributions to superannuation funds” that relate to an employee carrying out research and development activities on behalf of the company. Finally, “contributions to superannuation funds” in relation to an eligible company, means under s 73B(1), expenditure that would be allowable as a deduction to the company under s 82AAC of ITAA 1936. In this case, the contributions made for the employee in question were below the age based deduction limit applicable to the employee, so the contributions were deductible under s 82AAC.

Draft Taxation Determination TD 2006/D3

This Draft Determination relates to the tax treatment of superannuation pensions and annuities subject to family law splitting agreements or court orders. The Commissioner outlines the method he will use under s 27H(3) of ITAA 1936 to determine the tax-free deductible amount in relation to a superannuation pension or eligible annuity split pursuant to a family law agreement or court order.

Broadly, where a non-commutable superannuation pension or annuity (for example, a lifetime pension or annuity) satisfies the conditions set out in the Draft Determination, the Commissioner will split the deductible amount between the member spouse and the non-member spouse in the same proportion as the family law payment split.

However, if the terms and conditions of the pension change as a consequence of the marriage breakdown (ie, where the original pension was reversionary and subsequent to the marriage breakdown the pension ceases to be reversionary), a different method will be used.

In that case, the deductible amount of the original pension will be recalculated assuming that the circumstances that exist immediately following the split had existed as at the commencement date of the original pension.

Draft Taxation Determination TD 2006/D4

This Draft Determination also relates to the tax treatment of superannuation pensions and annuities subject to family law splitting agreements or court orders. The Commissioner states that a non-member spouse under age 55 is **not** entitled to a pension rebate under s 159SM or s 159SU of ITAA 1936 in respect of a superannuation pension or “eligible annuity” split on a specified percentage basis pursuant to a family law agreement or court order.

This is on the basis that ITAA 1936 provides that the recipient of a “rebateable amount” of an annuity or pension must be at least 55 years of age, unless the annuity or pension is a death or disability annuity/pension for the recipient. The amount of the rebate (where it is allowed) is 15%.