Manager
Retirement Benefits Unit
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

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Email: superannuation@treasury.gov.au

Dear Manager

#### Superannuation Reform Package - Exposure Draft – LRBA

IOOF Investment Management Limited (ABN 53 006 695 021 AFS Licence No. 230524) welcomes the opportunity to provide feedback to the Government on the exposure draft of the superannuation reform package provisions dealing with Limited Recourse Borrowing Arrangements (LRBAs).

IOOF supports the reforms to superannuation. We welcome the opportunity to provide feedback on the proposed Treasury Laws Amendment (2017 Measures No. 2) Bill 2017. Overall we are supportive of the intention behind the changes, to ensure the integrity of the transfer balance cap and total superannuation balance requirements. However we do have concerns as to the specific implementation of including debt associated with a limited recourse borrowing arrangement (LRBA) in a member’s total superannuation balance.

Our submission is attached,

Yours sincerely



Frank Lombardo

**General Manager – Client & Process**

# Submission to Treasury: IOOF feedback on exposure draft legislation

We welcome the opportunity to provide feedback on the proposed Treasury Laws Amendment (2017 Measures No. 2) Bill 2017: limited recourse borrowing arrangements.

Overall we understand and agree with the need to ensure the transfer balance cap and total superannuation balance systems cannot be exploited. However we do have concerns as to the specific implementation of including debt associated with a limited recourse borrowing arrangement (LRBA) in a member’s total superannuation balance.

**Inclusion of transfer balance credit for repayment of LRBA**

The proposed transfer balance credit created where the repayment of debt under a LRBA results in an increase in a member’s pension interest does not give rise for any major concerns. Such arrangements would appear to be clearly attempting to circumvent the transfer balance cap system and are rightfully and appropriately captured under the new rules.

**Inclusion of LRBA debt in total superannuation balance**

Including the proportion of a member’s interest in LRBA-related debt does not appear to achieve an equitable outcome when considering the overall design of superannuation law. Going forward it would appear that the use of a LRBA could in fact disadvantage individuals who are attempting to grow their superannuation savings to fund their retirement. Under the proposals, using a LRBA can result in an individual’s total super balance exceeding the general transfer balance cap, even though they have substantially less than $1.6 million saved to fund their retirement.

For example, a member of a SMSF has a $1 million member balance in accumulation phase. This is backed by a $1.7m property subject to a LRBA with outstanding debt of $700,000. Given the debt must by its nature be repaid at some time, the member has $1 million of assets in superannuation to support their retirement. However the inclusion of the outstanding loan balance would result in a total superannuation balance of $1.7m and preclude the member from making additional non-concessional contributions going forward.

The proposal also creates ambiguity when moving a member with a LRBA into retirement phase. Continuing the above example, the value of the transfer credit created on establishing the retirement phase interest would be $1 million, despite the fact their total super balance for the same interest is $1.7 million. Compared to a different member who has the same net member interest, but does not have the LRBA, the LRBA-using member is severely impacted simply because of an investment choice – an investment choice which does not give rise to an inherent advantage to make additional contributions.

Given the nature of this change, it would be expected to only impact those who have member balances less than $1.6 million but on a gross basis exceed this figure. Members who have already accumulated in excess of $1.6 million may look to use a LRBA to enhance the growth of their existing assets, and can do so under the new law. As such this change is effectively targeted at those who are actively engaged in saving for their retirement and have, on a net basis, not reached the $1.6m threshold set as a reasonable level of assets to support their retirement. The very same group who should be able to benefit from making contributions and, where appropriate, investing in a LRBA to grow their funds.

Counting debt as an asset appears to be a fundamentally flawed concept – particularly as debts are expected to be repaid over time. This creates a circumstance where, as the outstanding debt reduces over time the member may be able to start re-contributing even though their total super balance (excluding debt) may actually be increasing due to investment earnings. In addition to this, with the release of PCG 2016/5 by the ATO it is clear that a related party loan funding a LRBA must be repaid on a principle and interest basis, otherwise the arrangement could be subject to the non-arms’ length provisions which provides a method for punishing those arrangements which may be designed to exploit the total super balance calculation.

Measuring an individual’s total superannuation balance on a gross basis is not commensurate with existing valuation principles, the way LRBAs operate or a superannuation system which is fair when comparing the funds people have set aside to fund their retirement. This change appears to be “taking a sledgehammer to crack a nut” in an attempt to pre-empt strategies which in practice would not have any significant ability to exploit the total superannuation balance rules over the longer term.

**Grandfathering of existing LRBAs**

Additionally, we note the amending bill includes provisions to grandfather existing borrowings in place before 1 July 2017. To help ensure existing funds using LRBAs have certainty that their existing arrangement will benefit from this grandfathering we would ask Treasury to clarify whether it is simply the borrowing associated with the arrangement which is grandfathered, or the arrangement itself.

If the policy intent is to grandfather existing users of LRBA arrangements, we would suggest this could be achieved by clearly stating that the arrangement is subject to grandfathering, not simply the borrowing. This would ensure existing funds are not constrained in their ability to administer their fund based on their existing loan arrangements. Such grandfathering could also ensure any refinanced loans as part of the existing arrangement must not exceed the existing borrowing if there is concern about using refinanced amounts from existing LRBAs to increase the level of debt within SMSFs to lower member balances.

It has been prepared on behalf of IOOF Investment Management Limited (ABN 53 006 695 021, AFSL 230524) based on information that is believed to be accurate and reliable at the time of publication.