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Law Design Office
Treasury
Langton Crescent
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Dear Treasury

**Miscellaneous amendments to Treasury portfolio laws 2020
Superannuation tax submission**

MLC Wealth Limited (**MLC**) is part of the National Australia Bank corporate group, and is responsible for the administration of two of the largest superannuation funds in Australia. Together, those funds have in excess of one million adult Australian members and in excess of $100 billion of assets.

MLC welcomes the opportunity participate in the consultation for the miscellaneous amendments to Treasury portfolio laws 2020 and provides the following submission on aspects effecting the taxation of superannuation. This submission is confined to the taxation of superannuation funds and will only comment upon that.

We are a member of the superannuation industry body, The Association of Superannuation Funds of Australia Limited (**ASFA**), and have had the advantage of reading the final draft of its submission.

We endorse what ASFA has said in its submission about its concerns with two key aspects of the proposed amendments effecting the taxation of superannuation. However, those two key issues are of sufficient importance that we feel compelled to also provide a separate submission to reinforce those concerns.

Statutory references in this submission are to the *Income Tax Assessment Act 1997*.

***Items 93-95 – extension of the non-arm’s length income rules, including retrospective operation***

We note para 1.98 and 1.99 of the draft explanatory memorandum explains that the proposed amendment to s.118-320 is to close an unintended legislative drafting oversight that meant capital gains made by complying superannuation funds on segregated current pension assets were tax free, even if the gain was non-arm’s length.

Whilst we are generally supportive of amendments to overcome unintended tax outcomes, we strongly oppose the proposed amendment in its current form because it will in our view create other unintended adverse tax consequences.

Specifically, we believe it can have an adverse tax impact where a superannuation fund merger occurs which relies on Division 310 CGT rollover of assets, both where the merger is in the future and where it has already occurred, thereby in effect causing a retrospective tax liability.

When the closing fund transfers its assets to the successor fund, rather than realising capital gains on those assets at that time (which would be a cost impediment to the merger), the successor fund inherits the cost base of the assets from the closing fund under the Division 310 rollover. Generally, that will mean that the successor fund will have a lower cost base in those assets than if it acquired them on-market at the time of the merger. The result is that later (perhaps years later) the successor fund will make a larger calculated capital gain when it sells those assets due to their lower cost base. There is no mischief in that, and if the assets sold are segregated current pension assets, the sale will be tax free under the current s.118-320 (and so it should be). However, the unintended effect of the proposed amendment will be to deny the s.118-320 CGT exemption in many of those cases.

This tax risk is potentially very large given the large scale of fund merger transactions. It could impact all the segregated current pension assets rolled over. The risk is particularly acute where the merger is between superannuation funds that have the same trustee, which due to having a single legal identity, may necessarily be unable to deal at arm’s length with itself in performing the merger.

Ultimately, creation of undue CGT costs and risks on Division 310 rollovers by this amendment in its current form may frustrate the Government policy to reduce barriers to merge funds where it enhances scale efficiency. The end-result may be reduced retirement outcomes for many Australians.

If the amendment will proceed, we therefore kindly request that it be accompanied with a complimentary amendment to expressly preserve the s.118-320 CGT exemption for assets acquired by a successor fund under Division 310 rollover, and without tax at 47% under the non-arm’s length income rule in s.295-550 applying.

***Item 97 – change to deductibility of temporary incapacity insurance benefits***

**Retrospective change to deny a deduction for temporary incapacity insurance benefits paid from a superannuation fund**

There are two schools of thought about how periodic temporary incapacity insurance receipts from policies owned by a complying superannuation fund that are on-paid to sick and injured members are taxed within the superannuation fund.

One school of thought is that the receipt is not assessable and the on-payment non-deductible. The other is that the receipt is assessable and the on-payment deductible. Importantly, both schools of thought involve tax neutrality for the superannuation fund, so by and large it does not matter which approach has been adopted. The tax outcome is largely the same.

However, with this proposed amendment to s.295-495 to deny a deduction, Treasury is picking and prescribing one school of thought over the other, and doing so with retrospective effect back to 1 July 2007. It is an unbalanced amendment that creates tax risk for superannuation funds to explicitly deny the deductions, without also providing certainty on the other side that the receipt is non-assessable.

We therefore strongly oppose the proposed amendment to s.295-495 in its current form. If the amendment will proceed, then the necessary certainty that the receipt is non-assessable should also be provided. The current CGT exclusion in item 7 of s.118-300 (inserted in 2015 with retrospective effect back to 2005) for receipts from injury and illness insurance policies is insufficient to provide that certainty because it does not exclude temporary incapacity insurance proceeds received by the superannuation fund on revenue account.

In addition, a change to deny a tax deduction should not be retrospective back to 1 July 2007. It should be prospective only. Although both schools of thought produce the same neutral tax outcome for the on-payment itself, application of the assessable/deductible approach will have meant that a greater number of tax deductions for expenses were available. For example, superannuation fund expenses for managing temporary incapacity insurance claims would be deductible where incurred to derive assessable temporary incapacity insurance receipts. Therefore, the assessable/deductible approach should not be abolished on a retrospective basis.

Thank you for your consideration of our submission.

Yours sincerely

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