
Trustee Corporations Association of Australia

**Comments on
Simpler
Super**

**Submission to
Treasury**

August 2006

Introduction

The Trustee Corporations Association (TCA) is the peak representative body for the trustee corporations industry in Australia. It represents 17 organisations, comprising all 8 Public Trust Offices and the great majority of the 11 private statutory trustee corporations (see Attachment).

The TCA is pleased to have the opportunity to offer comments on *Simpler Super: A Plan to Simplify and Streamline Superannuation*.

The recommendations made in this submission aim to increase the longevity of the superannuation resources of severely disabled persons in order to provide an adequate level of care, without the long term reliance on the public health and welfare system.

Comments

We strongly support the Government's aim of removing many of the current complex tax arrangements and restrictions that apply to people's superannuation benefits. The proposed changes will give many individuals greater flexibility as to how and when to draw down their superannuation in retirement.

However, there are two matters in relation to people's ability to enjoy the benefits of the superannuation regime which we feel warrant attention.

One of the core services provided by trustee corporations involves managing the financial affairs of people who are unable to do so themselves due to lack of intellectual capacity.

Those people include victims of various types of accidents who are awarded large compensation payments due to the severe nature of their injuries. Such payments can amount to many millions of dollars as they are usually intended to provide for their lifetime care.

The injured person, for example, may only be 25 years old and, despite suffering intellectual incapacity as a result of an accident, could be expected to live for another 45 years. Apart from requiring ongoing medical care, there will often be a need for large sums to be spent on modifying the person's existing house or acquiring suitable new accommodation to facilitate wheelchair access etc.

In these circumstances, it has often been the practice of trustee corporations to place compensation money (or part of it) into superannuation and commence an income stream as an element of a prudent and tax effective investment plan for the disabled client.

Our two concerns in relation to current / proposed superannuation arrangements are detailed below.

1. Undeducted contributions cap

To ensure that access to the concessional taxed superannuation system is appropriately targeted, the Budget proposed a cap of \$150,000 a year on the amount of undeducted contributions that a person can make in a superannuation fund.

The Government subsequently announced that the cap can be averaged over 3 years to accommodate large 'one-off' payments of up to \$450,000 by individuals.

This concession generally will be helpful to people transitioning to retirement - for example, those who may have sold a property as part of their retirement planning – while preventing the system from being merely the preserve of the wealthy.

However, this approach will have a detrimental impact on severely disabled people by significantly reducing the longevity of their compensation payments.

This is because the proposed limit on undeducted contributions often will not be sufficient to appropriately accommodate the prudent investment of that money.

We believe that special consideration needs to be given to these disadvantaged members of the community, who are relatively few in number but who have already suffered greatly through their injuries.

To address this presumably unintended consequence of the proposed changes to the superannuation framework, we recommend that the Government give consideration to the following 2 options:

Option A

This approach would involve removing the UDC cap for individuals who meet the 'permanent incapacity' definition set out in regulation 6.01(2) the *Superannuation Industry (Supervision) Regulations 1994*, which states:

"permanent incapacity, in relation to a member who has ceased to be gainfully employed, means ill-health (whether physical or mental), where the trustee is reasonably satisfied that the member is unlikely, because of the ill-health, ever again to engage in gainful employment for which the member is reasonably qualified by education, training or experience."

Option B

An alternative approach, for persons who meet the 'permanent incapacity' definition, would be to introduce an aged based UDC cap linked to the number of years until normal retirement age (ie 65 years).

This calculation could be based around the principles applying to the calculation method for the post June 1994 invalidity component under Section 27G of the *Income Tax Assessment Act 1936*.

This approach would give younger individuals a greater capacity to contribute to superannuation, whilst older individuals could take advantage of this method or the normal UDC rules as stated in the Treasurer's 13 June 2006 press release.

This concept is illustrated in the following two examples.

Example 1: Ben, aged 38, has received a compensation payment of \$2,500,000 due to a motor vehicle accident whilst cycling at lunchtime. Using this alternative approach, he would be able to contribute up to \$4,050,000 into superannuation (ie 65 less 38 x \$150,000 UDC cap) and could gain access to the funds under the permanent incapacity definition.

Example 2: Carroll, aged 63, was injured whilst gardening at home. Given the extent of her injuries, she satisfies the permanent incapacity definition. Using this alternative approach, she would only be able to contribute up to \$300,000 into superannuation (ie 65 less 63 x \$150,000 UDC cap) which is consistent with the operation of the \$450,000 UDC cap.

The TCA recommends that Option B be adopted. We feel that this would be the fairer approach, providing an alignment of the longevity of a disabled person's capital with their life expectancy.

We acknowledge that the potential for abuse of the concession (under Option A or Option B) would be a concern for the Government.

Under current payment standards, the requirement to seek medical certification or some verification concerning the termination of employment is not specifically stated in the SIS regulations. The trustee needs only to form the opinion that a member meets the definition of 'permanent incapacity'.

We recommend that substantiation procedures be tightened to address this concern.

A case study shown in Attachment 2 illustrates the substantial increase in tax payable where a large court awarded compensation payment is unable to be invested in the superannuation framework versus within that framework. The difference could mean a significantly lower standard of care for the injured person, whilst increasing the family's burden to meet the shortfall.

2. 'Permanent incapacity' and access to allocated pensions

We are also concerned that the proposed reforms of the superannuation regime do not address an anomaly in the *SIS Regulations* which results in discrimination against people who acquired a severe disability at a young age.

Schedule 1 of those regulations provides that there are no cashing restrictions in relation to fund members suffering 'permanent incapacity' (as defined above).

However, we understand that interpretation of that definition by a majority of the superannuation industry and by the ATO is that a member of a superannuation fund who has never commenced gainful employment is ineligible for early release of funds, in the form of an allocated pension, ahead of the normal 'preservation age'.

We believe that such discrimination unfairly impacts on the standard of care and quality of life that those disabled persons are able to enjoy.

Although we do not have hard data, we suggest that only a small number of people would fall into this category. Without a change in policy, they will be taxpayers for most of their lives, and will not benefit from the Government's Budget

announcement of tax free income streams for over 60 superannuation investors, post 1 July 2007.

We recommend that this situation be addressed by amending the above definition to refer to a person's inability to engage in gainful employment, rather than to 'ever again' do so.

Such an amendment would affect relatively few people, and would not represent a threat to the integrity of the superannuation system.

Nor would such an amendment affect the recommendation in section 1 of this submission.

Attachment 1

Trustee Corporations Association of Australia Members

- ANZ Executors & Trustee Company Ltd
- Australian Executor Trustees Ltd
- Elders Trustees Ltd
- Equity Trustees Ltd
- National Australia Trustees Ltd
- Perpetual Ltd
- Public Trustee for the ACT
- Public Trustee New South Wales
- Public Trustee for the Northern Territory
- The Public Trustee of Queensland
- Public Trustee South Australia
- The Public Trustee Tasmania
- Public Trustee Western Australia
- Sandhurst Trustees Ltd
- State Trustees Ltd
- Tasmanian Perpetual Trustees Ltd
- Trust Company of Australia Ltd

Attachment 2

Case Study

Anthony, who is now aged 45, was awarded a compensation payment of \$4,000,000 (after legal costs and past care payments) as a result of severe injuries suffered in a motor vehicle accident.

Anthony's wife does not work as she provides the majority of his care and cares for two school age children. Anthony does not have any superannuation in place (for the sake of simplicity).

Anthony first spends \$800,000 to renovate his home to meet his new requirements as he is wheelchair bound and requires daily therapy. Leaving aside approximately \$200,000 in Anthony's name for general liquidity and expenditure for the first year, and assuming our recommendation in the main body of this submission is adopted, an undeducted contribution of the remaining \$3,000,000 could be made into a DIY Superannuation Fund.

Anthony and his family require approximately \$180,000 per annum (indexed at 2.5% per annum) to meet their living expenses (not including management fees and taxes).

On the basis of permanent incapacity, Anthony is eligible to access his superannuation funds immediately and an income stream is commenced in the form of an allocated pension. Anthony receives a 15% rebate on the pension as he is less than 60 years of age. Once he reaches 60 it is assumed there is no tax on his pension income (in line with proposed legislation).

The level of pension taken is adjusted annually based on the increase in Anthony's requirements. Once the maximum pension amount is reached, commutations are made to ensure Anthony and his family have the requisite funds to meet their needs. Using this strategy, Anthony's compensation funds run out in the 35th year, which is aligned to his life expectancy.

Alternatively, if the possibility of making the large undeducted contribution was not available, all the funds would be invested in Anthony's name and the deficit between income generated and expenditure would be covered by the sell down of assets, which in turn would generate capital gains.

Under this scenario, Anthony's funds would be exhausted in the 30th year. This means that he would no longer be able to meet his requirements and would be forced either to: borrow money; sell his home, downsize and release some capital; or, rent until his death¹.

The different outcomes under these 2 scenarios is summarised in the following table.

	Invested in Anthony's name	\$3,000,000 Undeducted Contribution
Available net funds	\$3,200,000	\$3,200,000
Life expectancy	35 years	35 years
Total tax paid (entire period)*	\$1,172,390	\$575,025
Portfolio exhausted	In 30 th year	In 35 th year

* 2005/2006 tax scales.

Note: Anthony's ability to access Centrelink payments will depend on the preclusion period set by Centrelink. In our example we have assumed that Anthony's preclusion period is beyond his life expectancy and as such he does not receive any payments. Considering Anthony's age and the amount of the compensation payment, this is a reasonable assumption.

¹ Renting is often not a viable option as the client often has certain specific requirements (hoists in bathrooms, wide halls etc).