APPENDIX F : GOVERNMENT RESPONSES TO THE ISSUES RAISED BY THE AUSTRALIAN DEMOCRATS

1. GENERAL

1.1 Prudential supervision: The Australian Democrats request a clear and specific commitment from the Government on the Senate Select Committee Report on *Safeguarding Superannuation*

GOVERNMENT RESPONSE

The Government on 4 June 1992 welcomed the Committee's report and announced its intention to develop a detailed package of measures concerning prudential supervision for introduction to Parliament in the forthcoming Budget Sittings. It is important in developing that package that the Government be able to consult with the industry, and bodies such as the Institute of Actuaries of Australia, so that a balance is achieved between the costs and benefits to contributors of enhanced prudential supervision. The Government is also required to consider other important reports (such as those of the Industry Commission and the Australian Law Reform Commission) which have made recommendations on matters canvassed in the Senate Select Committee's report.

But the Government is able to indicate the direction it wishes to follow in considering the recommendations of the Senate Select Committee on Superannuation report *Safeguarding Superannuation*, released on 4 June 1992.

The Committee recommends that the ISC become the sole regulator of superannuation products, but that it liaise and co-ordinate with the RBA, ASC and TPC.

This recommendation accords with the Government's announcement in the 1991-92 Budget on the role of the ISC and with the Treasurer's announcement of 5 June 1992, on the Government's response to the Martin Committee, that a Council of Financial Supervisors would be established to improve the consultative links between financial supervisors. This Council would comprise officers of the RBA, ISC and ASC, and would meet at least biannually and would be chaired by the RBA.

The Committee recommends that the main duties and responsibilities of trustees and directors of corporate trustees be clearly spelt out in the Occupational Superannuation Standards Act (OSSA).

The Government supports the codification of certain trust law principles for inclusion in that Act. Detailed proposals on this are being developed for the Government's consideration.

An industry fidelity fund be established to protect members in the event of fraud.

The Government is considering the issue of fidelity funds; the feasible coverage of such funds; whether industry coverage should be voluntary or compulsory; the likely costs and benefits of such funds; and the changed expectation and behaviour which might result from such funds. It is not yet in a position to respond to this recommendation.

The OSSA be altered so that

(i) the ISC can impose civil and criminal penalties;

(ii) trustees and directors can be removed where they are not fulfilling fiduciary obligations;

(iii) civil proceedings can be instituted by the ISC against trustees on behalf of members.

Recommendations (i) and (ii) are consistent with the Committee's recommendation on codification (see above) which the Government supports. The precise nature and extent of the enhanced powers to be proposed for the ISC would need to minimize the prospect of subjective action by the ISC and to reduce intrusion by the ISC on the normal responsibilities of members towards their trustees and directors. Recommendation (iii) does affect these responsibilities and the Government would wish to consider that issue further and in the context of the powers and duties of other regulators, such as the TPC.

The Committee recommends that the requirement for equal employer/employee representation should apply to all funds with 5 or more members (cf the current threshhold of 200 members or more).

The Government agrees to the appropriateness of a lower threshhold for equal representation – or the appointment of an independent trustee. It will examine such a lower threshhold in terms of its practicalities and costs for members.

The Committee recommends that a central fund be established for unclaimed benefit funds (or inactive accounts) with its administration tendered out by the Government on a fee for service basis.

The Government agrees that a central fund could be appropriate to reduce the costs faced by individual funds in managing inactive accounts. It proposes to consider detailed arrangements for such a fund.

The Committee recommends:

(i) that members approve a repatriation of a surplus in a defined benefit scheme to the employer;

(ii) various rules be applied to defined benefit funds regarding, for example, the maximum size of a surplus and a minimum ratio of assets to liabilities.

These recommendations require detailed consideration eg. as to the liability of employers for defined benefits; the role of any employee contributions in meeting defined benefits;

and the appropriateness of a minimum funding standard. A Government response to the recommendations would need to be informed by these technical considerations. In general, however, the Government can support a requirement that members be consulted before major changes to their funds are effected, eg. as to the disposition of any surpluses.

The Committee recommends that the funds maximum investment in in-house assets be reduced from ten per cent to five per cent.

The Government supports the basis of the Committee's recommendation and has asked that detailed proposals to improve the integrity of the in-house assets rule be developed for its consideration.

The Committee recommends that trustees who act as investment managers of superannuation funds be required to hold dealers' licences.

The Government accepts that such trustees should be treated consistently with the treatment of other investment managers who are required to hold a dealers' licence.

The Committee's majority recommendations in the investment area are that:

(i) no investment controls be placed on superannuation fund investments

(ii) the matter be re-examined within three years.

Its minority recommendation is that a National Development Fund be established with one per cent of superannuation fund assets for directed investment for the development of new technology and for patient development capital for smaller firms and that no more than 20 per cent of assets of superannuation funds be invested off-shore.

The Government announced in 'One Nation' in February 1992 the establishment of programs for the development of new technology and for patient capital. In particular, the pooled development fund initiative is specifically directed at the sorts of investment of concern in the minority recommendation. In designing this measure, the Government has deliberately set up a mechanism that will encourage superannuation gunds to invest in these areas. The Government is willing to consider further refinements to the pooled development funds measure if necessary. Consistent with its earlier statements, the Government prefers to use incentives for these purposes rather than directing members' funds in order to support the broader goals of society. Any such direction would give rise to claims that members' funds are not being maximised for their intended purposes – members' retirement incomes – and/or are being subjected to unduly high risk.

The Committee's main recommendation on the scope of the superannuation industry is that the Government support increased competition by supporting new entrants.

The Government supports increasing efficiency through increased competition and is considering the role of bank account superannuation and superannuation savings accounts in this context.

The Committee recommends that:

(i) all funds formalise internal dispute resolution mechanisms;

(ii) the establishment of an external dispute resolution mechanism.

Proposals are being developed in response to the Government's intention (announced in the 1991-92 Budget) and the Committees' recommendations on this matter. The Government then intends to consult with industry on a proposed approach to dispute resolution.

The Committee recommends that the Government seek wider powers over superannuation and legislate relying on a combination of taxation, corporation and pension powers.

This recommendation is in accord with the Government's 1991-92 Budget announcement. The Government is obtaining legal advice on the matter and will respond after that advice has been considered.

1.2 Preservation age: The Australian Democrats propose setting the preservation age at 60, except for occupations with a lower statutory retirement age. The Australian Democrats suggest that the preservation age could be phased in over, say, 15 years.

GOVERNMENT RESPONSE

The Government intends to replace the current preservation arrangements with provisions requiring all future superannuation benefits to be preserved to the preservation age after 1 July 1993

- this measure will increase substantially the proportion of superannuation savings that are subject to preservation.

The Government is also willing to consider increasing the preservation age, so that by 2025 virtually all superannuation benefits will be preserved to age 60

- some flexibility in the access to superannuation benefits allowed between the ages of 55 and 60 would also be considered.

1.3 Taxation of lump sums: The Australian Democrats propose setting a maximum (indexed) lump sum amount.

GOVERNMENT RESPONSE

The Government proposes to announce in its Superannuation Simplification Policy new arrangements for reasonable benefits limits. These arrangements will include an indexed fixed dollar cap on the lump sum RBL, together with transitional arrangements.

1.4 Taxation of contributions: The Australian Democrats propose taxing contributions at different rates depending on the income of the member. In particular, they propose exempting low income earners' contributions and applying higher rates of tax to higher income earners' contributions.

GOVERNMENT RESPONSE

The Government considers that it would be extremely difficult to administer a system of varying rates of tax on employer contributions, depending on the income of the employees on whose behalf the contributions were made. Such a system would add significantly to the administrative and compliance costs of the SGC, which would result in lower retirement incomes. Moreover, differences in tax rates applied to employer contributions would open avenues for tax avoidance.

The Government is, however, willing to consider other ways to ameliorate the impact of fund charges and taxes on small contributions. For example, the Government will consider measuring compliance with the SGC on a quarterly basis and lifting the income threshhold from $250/month.

1.5 The Australian Democrats propose that the Government should address the alleged bias against self-funded retirees in respect of income tax and fringe benefits.

GOVERNMENT RESPONSE

The income tax system is not biased against self-funded retirees. Indeed, self-funded retirees have often benefited from substantial tax concessions during the period that they have accumulated their retirement savings.

The Government is examining a range of issues that relate to the tax and social security treatment of retired persons in the Budget context.

2. SGC SPECIFIC

2.1 Impact on employment: Senator Kernot requests answers to questions, on the impact of introducing the SGC at the rate of 4 per cent for large businesses and on changing the small business threshhold to $1 million or $1.5 million, she asked in the Senate Select Committee's hearings.

GOVERNMENT RESPONSE

The answers to Senator Kernot's questions will be provided to the Senate Select Committee's Secretariat on 15 June 1992.

2.2 The Australian Democrats propose moving the system from a monthly basis to a quarterly basis from 1 July 1993.

GOVERNMENT RESPONSE

The Government is willing to adopt a quarterly system for the SGC from the 1993-94 year. Under this system, employer superannuation support would be measured on a quarterly basis. The employer would be expected to provide the prescribed minimum level of superannuation support during the quarter or within 28 days of the end of the quarter

- this system would not override monthly compliance obligations that may arise under an award superannuation provision.

2.3 The Australian Democrats think that the exemption threshhold ($250/month) can stay if:

- there is a limit placed on the administration fees funds can charge;
- insurance is made voluntary; and
- contributions are exempt where they are made on behalf of low income earners.

GOVERNMENT RESPONSE

The Government is not attracted to requiring superannuation funds to cross subsidise members according to their incomes by placing a cap on administration fees.

The SGC does not require insurance. The Government understands that insurance is voluntary in some funds.

The Government believes that it would be administratively complex to apply different rates of tax to employer contributions depending on the incomes of the employees on whose behalf the contributions are made. Moreover, multiple rates of tax would open up avenues for tax avoidance. For these reasons, the Government is not attracted to exempting contributions made on behalf of low income earners.

In these circumstances, the Government believes that a more appropriate method of addressing the concerns raised by the Australian Democrats would be to consider lifting the exemption threshhold to $450/month.

2.4 The Australian Democrats propose that the SGC legislation be amended in order that flat rate enterprise (or industry) superannuation awards be allowed to override the requirement that the superannuation guarantee percentage be contributed for each individual employee. This would only apply where the employer's total contributions are larger than or equal to those that would apply under the SGC.

GOVERNMENT RESPONSE

It would be extremely difficult to administer a system that allowed flat dollar employer contributions based on the aggregate SGC obligation across all of an employer's employees. The Government believes that administrative factors would not permit such a system.

2.5 **The Australian Democrats seek much more clarification on the linkages between increases in the SGC and future wage negotiations.**

GOVERNMENT RESPONSE

The Government has previously indicated that, on present information about inflation, earnings growth and output growth, there would appear to be room for a national wage increase and the SGC over the course of 1992-93, consistent with its inflation target.

However, the Government has given no commitment on the timing of a national wage increase or the quantum of such an increase. It observes that the ACTU has not formulated a claim and there have been no discussions with the Government on timing or quantum.

The Government has also indicated that the provision of additional superannuation under a Superannuation Guarantee Charge would be taken into account by the Government in determining its attitude on a national wage increase. Thus, for example, should a national wage increase be granted which was inconsistent with the Government's view of the economy's capacity to absorb that increase, the Government retains the option to ask the Parliament to legislate more modest SGC provisions than those now planned.

The provision of further details on the linkages must, however, await the formulation of a proposal which is specific as to the timing and quantum which proposals can be assessed in light of the Government's relevant economic forecasts.

That assessment would be guided by information already provided to the Australian Democrats that, on even modest forecasts of productivity growth, the implementation of the SGC over the decade will equal only one third of expected productivity gains.

Furthermore, on an assumption of a full offset in wages to the SGC, there would be negligible employment losses with an SGC of 5 per cent.

While employment losses would be encountered on the hypothetical and extreme assumption that 5 per cent SGC would add fully to unit labour costs, that assumption is entirely contrary to the Government's stated policy and to the productivity forecasts noted above.

2.6 **The Australian Democrats seek a Government commitment that community services such as HACC, child care, etc will receive supplementation to cover the SGC, so that services are not cut.**

GOVERNMENT RESPONSE

Costs such as superannuation contributions are routinely taken into account in examining the efficiency of programs such as HACC. Supplementation must take into account productivity and efficiency gains, changes in prices of other inputs, etc. This suggests that a dollar-for-dollar supplementation is neither feasible nor desirable. Nevertheless, the total remuneration of employees, including superannuation contributions stemming from the SGC, will be taken into account in relation to the funding of projects in these programs.

2.7 **The Australian Democrats propose that the SGC, interest and the ATO's administrative fee be tax deductible in the following circumstances:**

(a) **where the employee refuses to join a superannuation fund so that the employer cannot discharge an SGC liability;**

(b) **where the employee leaves during the first year and the employer cannot make qualifying contributions for whatever reason; and**

(c) **where the fund to which contributions have been made is not a complying fund and the employer could not reasonably know of this – subject to vesting to protect the employee.**

GOVERNMENT RESPONSE

(a) Whether or not an employee can in fact refuse to join a fund depends on the rules of the particular fund. In some cases, where an employer makes contributions on behalf of an employee, the employee is automatically and irrevocably a member of the fund. In other cases, employees can refuse to join a fund, simply by refusing to fill in a form

- in these circumstances, the employer always has the option of making contributions to another fund.

The Government is examining this issue in the context of prudential supervision of superannuation funds.

(b) The Government is drafting amendments to the Occupational Superannuation Standards legislation to enable employers to make contributions on behalf of former employees

- such contributions would be tax deductible to the employer.

c) The Government is drafting an amendment to the Occupational Superannuation Standards legislation that will ensure as far as is practical that SGC contributions will not be made to non-complying superannuation funds

– the Insurance and Superannuation Commission will publish a list of complying funds.

2.8 **The Australian Democrats propose that certain companies be treated as small employers, irrespective of their annual payrolls: for example, group training companies and labour hire firms.**

GOVERNMENT RESPONSE

The Government sees no reason to treat labour hire firms differently from other employers. To provide a special provision for such employers would cut across tax equity and neutrality objectives and would not sit well with the Government's retirement incomes policy. Moreover, any such special provision would involve difficult boundary issues; for example, such a firm could be a part of a larger company group.

It is also aware that, in law, the Government is unable to distinguish between group training companies and other like companies. The Government would consider providing grants to reduce any difficulties which affect group training companies.

2.9 **The Australian Democrats propose that:**

- **local government councillors be exempt from the SGC unless they are on normal salaries; and**
- **the contractors provision be clarified.**

GOVERNMENT RESPONSE

Local Government Councillors

The Government intends moving an amendment to the SGC legislation to remove a technical defect that seemingly brings local councillors automatically within the definition of 'employee'. The Australian Taxation Office has advised that the word 'payment' in the relevant clause of the Bill be changed to the word 'remuneration'

- this amendment will result in local councillors who receive salary or wages being covered by the Superannuation Guarantee. Other local councillors, who typically receive a monthly payment for attending meetings, will not be covered by the Superannuation Guarantee.

Contractors

The Commissioner of Taxation will issue a ruling on the whole issue of who is an employee and who is an employer shortly after the legislation is passed. This ruling should go a long way to resolving the uncertainties about this matter.

The following comments are offered to assist the Australian Democrats in understanding the provision.

Background

Clause 12(3) of the Superannuation Guarantee Bill includes as 'employees' persons who work under contract that is wholly or principally for their labour. The provision is designed to include a person who may not be an employee in the normal sense but who is in fact not very distinguishable from an employee.

Under subclauses 11(2) and 12(11) of the Bill, salary or wages paid to a person who works 30 hours or less per week, where that work is wholly or principally of a domestic or private nature, is not taken into account for superannuation guarantee scheme purposes.

Contract

Whether someone is a contractor rather than a common law employee will be a question of fact. The Commissioner of Taxation's view (see IT 2129) is that a contractor, as distinct from an employee, is someone who:

- Is contracted to perform a specific task within a specific time for an agreed amount of money;
- otherwise has freedom in the way the task is performed;
- doesn't have the normal entitlement of employees, such as leave and sick pay;
- normally renders accounts payable by invoice;
- bears the responsibility, and liability, for losses;
- generally is not eligible for workers' compensation from the principal;
- generally will be available to perform services for the public at large.

The mere fact that someone is a contractor does not mean that clause 12(3) will apply. That will depend on whether all the tests in 12(3) are satisfied (see below).

Wholly or Principally

The Commissioner of Taxation's view is that a contract is principally for labour where the labour content exceeds 50 per cent of the value of the contract (see IT 2129). The Commissioner would not simply accept the values the parties to the contract assigned to each of its elements. Instead, he would use a market based apportionment made in the context of the contract's overall value.

For Labour

'Labour' is not defined in the Bill. The usual position is that labour means work of a physical nature. But the courts tend to take a wider view of this context and include work which is physical, mental or artistic (DFCT v Bolwell (1967) 1 ATR 862).

Whose Labour?

Subclause 12(3) requires the contract to be for the labour of the person who works under the contract.

In Neale v Atlas Products (Vic) Pty Ltd (1955) 10 ATD 460, the High Court decided (at p461) that, if the contractor is free to engage others to perform the work for him, the contract is not for his labour. This is so even if the contractor actually did perform the work himself and had no intention of doing otherwise.

Amendments have limited the scope of this decision in the PAYE context. But there are no similar provisions in the Superannuation Guarantee Bill.

Accordingly, subclause 12(3) would apply only where the contract, either expressly or impliedly, required the work to be done by the party to the contract.
Professionals

Accountants and lawyers are concerned that they may be treated as employees of their clients for the purposes of the Superannuation Guarantee Legislation.

This concern seems to be unfounded. In Bolwell, the court said that professionals are not employed under contracts for labour because their efforts result in something of their own creation, defined and limited according to their talents. People employed under contracts for labour are those employed to achieve a result determined or defined by someone else.

Partnerships

Another issue that has been brought to the Government's attention concerns whether a partner, who performs work under a contract entered into by the partnership, can be said to be an employee of the other party.

One view is that, because the Bill says that it applies as if a partnership were a legal person, a fictional entity is inserted between the principal and the partners so that they cannot be the principal's employees. A consequence of this view would be that forming 'husband and wife' partnerships could become a common avoidance technique. Another may be that partners would effectively be deemed to be their own employees.

The other view is that the Bill does not say that it applies as if a contract with the partners were a contract with a separate legal entity. The consequence of this view would be that a partner who performs work would be treated as an employee of the principal.

This would probably not affect large professional partnerships, because it is difficult to envisage cases where the work would be required to be done by a particular partner. So the contract would not usually be one for that partner's labour.

The Australian Taxation Office is examining the issues raised by this debate.

The Pay As You Earn (PAYE) and Prescribed Payments (PPS) Systems

The Superannuation Guarantee Bill generally requires superannuation contributions to be made for people employed to work under a contract wholly or principally for their labour.

The PAYE system extends to payments made to a person under a contract principally for the labour of the person to whom the payments are made unless they are covered by PPS.

For a person to be covered by PPS, he or she must not be an employee at common law; must be employed under a contract which in whole or in part involves the performance of work; and must be in one of nine specified industries.

There may be some people who are not covered by the PAYE system who will be covered by the Superannuation Guarantee.

Common Law Employees

Many people who describe themselves as 'contractors' are in fact common law employees. Such people are covered by the Superannuation Guarantee, regardless of the contractors question.

2.10 The Australian Democrats propose that the large employer threshhold be lifted from $500 000 annual payroll to $1.5 million annual payroll.

GOVERNMENT RESPONSE

The Government sees good reason for the $500 000 large business threshhold: it is consistent with the Training Guarantee Scheme and is broadly consistent with similar threshholds in State payroll taxes. Nevertheless, the Government is prepared to consider lifting the threshhold to $1 million.

2.11 The Australian Democrats propose that the SGC be introduced in 1992/93 at the rates of 3 per cent for small employers and 4 per cent for large employers.

GOVERNMENT RESPONSE

In 'One Nation', the Prime Minister announced an altered SGC implementation schedule which extended for a further year the 3 per cent rate applicable to small businesses (that is, those with an annual payroll of $500 000 or less). Whereas it was announced in the 1991-92 Budget that a four per cent rate would be applicable in 1993-94 that has now been postponed to 1994-95.

While no changes were proposed in 'One Nation' for larger firms, the Government is prepared to countenance an easing of the transition costs for firms with an annual payroll of between $500 000 and $1 million. It is prepared to consider raising the small business threshhold for SGC purposes to $1 million thus allowing those medium sized firms a 3 per cent rate for 1992/93 and 1993/94 in place of the five per cent rate which they otherwise faced. (This would also allow those firms to meet a lower prescribed rate under the SGC until 1997/98, when the same rate is to be met by small and large firms.)

The Government considers that this, together with its approach to a national wage increase, discussed above, would be a sufficient response to the real concerns of Australian firms.