Level 2
95 Pitt Street Sydney, NSW 2000
Telephone 02 8223 0000
Facsimile 02 8223 0077
Email tia@taxinstitute.com.au
Website www.taxinstitute.com.au
ABN 45 008 392 372

13 February 2009

Mr Paul McCullough
The General Manager
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: cgt_super_roll-over@treasury.gov.au

Dear Mr McCullough

CGT rollover for complying superannuation funds with capital losses

The Taxation Institute of Australia ('Taxation Institute') is pleased to provide its comments in response to the Treasury's discussion paper *CGT rollover for complying superannuation funds with capital losses* ('Discussion Paper').

We note that the Discussion Paper is intended as a guide to the potential design of the proposal to provide optional capital gains tax ('CGT') rollover for complying funds with capital losses, announced by the Minister for Superannuation and Corporate Law on 23 December 2008.

The Taxation Institute strongly supports the Government's intention to provide CGT rollover relief as a means of reducing the barriers to the merger of superannuation funds. Set out below are the Taxation Institute's general comments on this proposal, followed by more specific comments on a range of issues identified by the Taxation Institute.

1. General Comments

When the proposed capital gains tax roll-over for complying superannuation funds with capital losses was announced by the Minister for Superannuation and Corporate Law, he indicated that

> [m]ergers of super funds can lead to improved economies of scale, including more cost effective services to members. In the current financial climate, it is important that potential barriers to a robust and efficient super industry are minimised…[l]imited CGT roll-over will assist super funds in a net capital loss position seeking to merge with other funds by preserving the CGT offsetting value of any net capital loss.

The Taxation Institute agrees that the merger of superannuation funds can benefit members and minimise barriers to achieving a robust and efficient super industry. However, we are concerned that the proposed roll-over may not facilitate mergers as it addresses only one of the tax impediments, being the extinguishment of unrealised capital losses and not other impediments including:

- increased income tax liability for the transferor fund from revenue and capital gains realised by the occurrence a merger; and

- the extinguishment of pre-merger realised revenue and capital losses of the transferor fund.

We therefore submit that there should be:

- a roll-over for assets on both revenue and capital account and irrespective of whether they are in a unrealised gain or loss position (refer 2.1 below);

- a transfer of any unutilised revenue and capital losses from the transferor fund to the transferee fund. If necessary for integrity reasons, restrictions could be imposed on the rate at which transferred losses could be utilised (refer 2.2 below).

We further submit that:

- roll-over should be available to all superannuation entities (incl. pooled superannuation trusts (PSTs) and the complying superannuation (CS) component of a life insurance company) and not as proposed be limited to the merger of a complying super fund with another complying super fund with at least five members (refer 2.3 below);

- roll-over should be available on a permanent basis and not as proposed be limited to mergers on or after 24 December 2008 and before 1 July 2010 (refer 2.4 below); and

- the deemed acquisition date of rolled-over assets should be taken to apply for all income tax purposes (e.g. for the purposes of the "holding period requirement" in respect of franking credits and loss testing by companies and trusts in which the transferor super fund had invested) and not just for the purposes of applying the CGT discount (refer 2.5 below).

The matters raised above are discussed further below.

2. Specific comments

2.1 Extension of roll-over to all assets

The roll-over relief as currently proposed is limited to assets with unrealised capital losses. We submit that roll-over should be extended to assets:

- on both revenue and capital account; and

- irrespective of whether they are in an unrealised gain or loss position.

In support of this we note that:

- an income tax liability resulting to the transferor fund from the disposal of revenue and capital assets under a merger would reduce the balances of its members and is thus a barrier to merger similarly to that which results from the extinguishment of capital losses;

- the extinguishment of unrealised revenue losses under a merger would reduce the balances of its members and is thus a barrier to merger similarly to that which results from the extinguishment of capital losses;

- this would be consistent with the roll-over provisions that have applied to superannuation funds in the past;

- roll-over of all (capital) assets would avoid the equity issues that may arise amongst members from the proposed "cherry-picking" of assets with unrealised realised capital losses, which

could give rise to equity issues in cases where all members do not share equally in all assets; and

- roll-over of all assets would be less complex and easier to implement than the proposed roll-over of specified assets with unrealised capital losses.

2.2 Pre-merger realised losses

The roll-over as currently proposed is only of unrealised capital losses. Therefore the value of any unutilised pre-merger realised revenue and capital losses of the transferor fund would be lost. This would be the case if the merger capital gains are less than the pre-merger realised capital losses. The loss of realised capital losses of the transferor fund would prima facie result in a decrease in the benefits of its members.

We submit that unutilised pre-merger realised revenue and capital losses of the transferor fund should be able to be transferred to the transferee fund. In support of this, we note that:

- the transfer of realised revenue and capital losses is consistent with the stated purpose of the roll-over as their extinguishment could result in a reduction of member balances, which in turn could act as a barrier to mergers and the attainment of a more robust and cost efficient superannuation industry; and

- if necessary for integrity reasons, restrictions could be imposed on the rate at which transferred losses could be utilised.

2.3 Extension of roll-over relief to other superannuation entities

The proposed roll-over relief is limited to the merger of a complying superannuation fund with another complying superannuation fund with at least five members.

We submit that the roll-over should also be available for other types of superannuation entities, notably pooled superannuation trusts (PSTs) and the complying superannuation class (CS class) component of a life insurance company. In support of this we note that:

- other types of superannuation entities are subject to income tax in a comparable manner to complying superannuation entities; and

- the stated policy criteria for granting roll-over is equally applicable to other types of superannuation entities.

2.4 Permanent roll-over relief

The roll-over as currently proposed is limited to mergers on or after 24 December 2008 and before 1 July 2010. We submit that there should be a permanent roll-over to facilitate the merging of superannuation funds. In support of this we note that:

- the number of times since 1998 when superannuation funds became taxable that a rollover has been introduced as a temporary measure for the purpose of enabling superannuation funds to merge and improve economies of scale supports the need for a permanent a roll-over;

- tax impediments should not be key factor in determining whether a superannuation fund should merge;

- in the absence of a permanent roll-over, superannuation funds may defer mergers in the expectation that another temporary roll-over will be provided in the future. This could delay improvement in economies of scale and therefore adversely impact member returns; and

- the provision of temporary roll-overs means that members may be disadvantaged if a merger occurs outside the time when roll-over is available.

2.5 Acquisition date

The roll over as currently proposed provides that assets will be taken to have been acquired by the receiving fund at the same time as the asset was acquired by the transferring fund, for the purposes of applying the CGT discount to a subsequent CGT event to the asset. We submit that the deemed acquisition date should be taken to apply for all income tax purposes, including:

- the holding period rule in section 160APHO(2) of the *Income Tax Assessment Act 1936*; and

- loss testing by companies and trusts in which the transferor super fund had invested.

If you would like to meet with representatives from the Taxation Institute or require any further information or assistance in respect of our submission, please contact Joan Roberts on 03 9611 0178 or the Taxation Institute's Senior Tax Counsel, Dr Michael Dirkis, on 02 8223 0011.

Yours faithfully

Joan Roberts
President