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Senate Economics Committee
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Subject: Inquiry into the Tax Laws Amendment (2009 Measures No. 6) Bill 2009

Dear Committee

This submission is only concerned with Schedule 2 of the Bill ie the capital gains rollover relief for merging superannuation funds.

We fully support the Government's proposals to provide rollover relief for merging superannuation funds. Under current legislation, a merging superannuation fund loses the ability to utilise its tax losses. This has been a major impediment to rationalisation of the superannuation industry as a merger would have an adverse impact on members' entitlements. Currently there are a number of significant rationalisations which are on hold pending the passage of this legislation.

We also acknowledge the willingness of the Government and Treasury to consult on this legislation and note that the Bill currently before Parliament includes significantly improved provisions compared to those included in an earlier discussion paper and an earlier consultation draft. These improvements address a number of practical problems which would have arisen under the earlier draft wording where appropriate relief would not have been available in many rationalisations. We particularly appreciate the time taken by Treasury officials in discussions with us regarding these practical issues.

However we do have some remaining practical concerns with the current Bill. We have made four recommendations below which we believe will maintain the intention and integrity of the Bill but will make its application clearer and more efficient.

Concern 1: Sunset date

The proposed rollover relief is only available until 30 June 2011. We highlight the importance of increasing efficiencies and reducing costs in the superannuation industry and that the need for relief will continue beyond 30 June 2011.

Unless rollover relief continues to be available passed 30 June 2011, then a significant barrier to efficiency will be re-introduced from that date. Once more it will be difficult for funds to merge due to the inability to utilise tax losses as this will have an adverse impact on member benefits.

We acknowledge that the Government has previously stated that this would be reconsidered following analysis of recommendations from the Henry Tax Review.

However, a fund merger is not an event that occurs overnight. Most mergers involve a considerable planning period which could often exceed 12 months. Hence by mid 2010, new considerations of merging superannuation plans for rationalisation purposes may need to be put on hold because it will not be possible to complete any merger by the cut-off date of 30 June 2011. (Alternatively, the merger process may be rushed leading to greater likelihood of errors.) If a merger does proceed, it may be necessary to abandon it at the last moment if it is not going to be finalised by the cut-off date. These problems will contribute to inefficiency.

We recommend that the proposed rollover relief be applied on an ongoing basis rather than ceasing at 30 June 2011.

Concern 2: One year rule

We note that there are basically two approaches for obtaining rollover relief under the Bill (which we have called rollover relief and loss transfer).

One approach (rollover relief in Subdivision 310-D) enables the assets to be transferred to the new fund without triggering a “deemed” sale and crystallising a capital gain or capital loss in the fund which is winding up. Utilising this option enables the new fund to take up the cost base of the assets as they applied in the fund which is winding up.

This is an appropriate approach however this option is only available if the transfer of members occurs in a single tax year. In our experience, transfer may often occur over two tax years either because it is performed in tranches for practicality reasons or because of last minute hitches that push the completion into the following year.

We note that the Bill includes special provisions so that members who cannot be transferred due to restrictions beyond the control of the trustee can be ignored. This addresses some of the concerns we had raised in the consultation process. Nevertheless, we consider that there will be other circumstances where a transfer can legitimately occur over more than one tax year and yet the single year requirement will mean that this rollover relief option will not be available.

We understand that the single year rule has been included to simplify the tax process. In our view, this is unnecessary and allowing transfers to be spread over more than one year will not unduly add to complexity.

In fact, it increases complexity and costs to funds. In particular, such a rule is likely to mean that mergers will need to occur in the middle of a tax year to minimise the risk of the transfer being spread over two tax years. Currently most mergers occur at the end of a tax year in order to minimise communication costs with it only being necessary for one of the old and new funds to provide a periodic statement in respect of the completed year. Where a merger occurs mid year, the old fund must provide a statement for the part year and the new fund will subsequently produce a statement for the balance of the year. This is a duplication of costs. Further, the tax loss resulting from these additional costs in the old fund will not transfer to the new fund. These costs will be passed onto members through higher fees/lower returns.

We recommend that the single year rule be removed or at least replaced with a more flexible rule (eg provided that the transfer has been completed within two tax years.)

Concern 3: Sale date

The second approach (loss transfer in Sub-division 310-B) for obtaining rollover relief enables the transfer of losses accrued before the last member transfers. This includes capital losses which are deemed to have arisen on the transfer of any assets to the new fund. Losses arising after the last member transfers cannot be transferred. This approach can apply irrespective of whether assets are transferred between the funds or whether the existing assets are sold and the resulting cash is transferred.

In some cases, the merger agreement will deem that the assets of the fund which is winding up are to be held in trust for the trustee of the ongoing fund as from the date the members transfer. However it may take several days before the ownership is formally recognised on share registers, by the custodian etc. In some cases this formal change of ownership will never occur as the asset will have been sold to a third party and the resultant cash will be transferred.

Such an approach leads to concerns, as it is unclear as to the approach the ATO will take in assessing when any resultant capital losses occurred – for example, will the ATO consider that the sale of assets occurred at the transfer date or at a later date when, for example, a change of ownership is formally registered.

If it is a later date, then it might be considered that the members have not transferred until the last asset has been transferred. As such, members may be considered to be members of both the old and the new funds for a short period. This creates a further problem due to the reporting requirements under Corporations Law as it will be necessary for both the old and the new funds to prepare periodic statements covering the same period. This is not only going to lead to additional costs but also to greater confusion for members.

Similar concerns arise where the old fund is selling its assets before transferring the resultant cash to the new fund and the sale of some assets is not completed until a day or so after the effective transfer of members.

We recommend that it should be possible for losses incurred by the old fund (after the last member transfers) relating to the realisation of assets and other costs associated with the transfer of members and the wind-up of the fund to also be transferred to a continuing fund.

Concern 4: Assets must transfer

In order to use the rollover relief approach, a condition that, for each transfer event, an asset must become an asset of the continuing fund (or a PST or life insurance company in which the continuing fund has an interest). In most fund mergers, many of the assets of the old fund are sold to a third party at or just before the transfer date. The resultant cash proceeds are then transferred to the continuing fund rather than the original assets. Whilst we do not believe it is the intention, the proposed 310-45(4) could be read as stopping the rollover relief applying in respect of other assets which are transferred to the continuing fund.

We recommend that the Bill be clarified to ensure that rollover relief can apply to assets transferred to the continuing fund, even if other assets have been sold to a third party.

If you have any queries, please contact me on 03 9623 5552.

Yours sincerely

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