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Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2005

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Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2005

Date Introduced: 26 May 2005

House: House of Representatives

Portfolio: Treasury

Commencement: Royal Assent or 1 July 2005, depending on the section.

Purpose

This Bill gives effect to announcements made by the Government during 2005 of measures to ease the administrative burden for business and employees in complying with the requirements of the Choice of Fund regime.

The Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2005 (the Bill) amends the:

- *Small Superannuation Accounts Act 1995*
- *Superannuation Guarantee (Administration) Act 1992*
- *Superannuation Industry (Supervision) Act 1993,* and
- *Retirement Savings Account Act 1997*.

This Bill also closes the 'Superannuation Holding Accounts Special Account' to new employer deposits from 1 July 2006.

Background

General Background

Since 1996 the Government has campaigned to give most employees the right to choose which superannuation fund receives the Superannuation Guarantee contributions made on their behalf by their employers. This policy was implemented by the *Superannuation Legislation Amendment (Choice of Superannuation Funds) Act 2004* (which received Royal Assent on 30 June 2004). The Choice of Funds regime commences on 1 July 2005.

The Choice Regime

Under the Choice regime most employees may:

- only using the specified form, select an 'eligible choice' superannuation fund to receive Superannuation Guarantee (SG) contributions made on their behalf
  - the definition of 'eligible choice fund' is quite broad and encompasses most complying superannuation funds
- again, only using the specified form, change their nominated fund at the end of every 12 month period. If the employer agrees, they may nominate a new fund at less than 12 month periods.

If the employee is satisfied with the employers 'default fund' they may decline the opportunity to choose a fund. If they do not at first choose a fund – they may do so at any later time.

An employer must give there employees (except those who are specifically exempt from the Choice regime – see below) the specified form to use when choosing a fund.

If the employee does not nominate a fund, the employer must choose an eligible choice fund (i.e. a default fund) to receive their SG payments. In most cases this will probably be the employer's current fund.

Under Section 32D of the *Superannuation Guarantee (Administration) Act 1992* (SG Act) the 'Superannuation Holding Accounts Special Account', administered by the Australian Tax Office, cannot be an eligible choice fund for the purposes of the Choice Regime.

Choice Penalties

Penalties apply to the employer if they fail to meet the Choice regime's requirements. However, these penalties are low, for example the maximum penalty is $500 per employee, per notice period. The Commission for Taxation can reduce the penalty, including to nil. Actions that may lead to a penalty can be:

- failure to provide the specified form within the required period, or
- making SG payments on behalf of an employee to a fund that is not that employee's chosen fund.

Exclusions from the Choice Regime

Generally, contributions made to the following funds are taken as being conformity with the Choice regime:

- commonwealth Government defined benefit funds
- certain private sector defined benefit funds[1]
- funds specified in State industrial awards
- funds specified in certain Victorian agreements

- funds prescribed in Commonwealth, State or Territory legislation, and
- funds specified under an Australian Work Place Agreement or Certified Agreement.[2]

This means that employees, who have contributions made on their behalf to such funds will not be offered the specified choice form and will not be able to choose a fund to receive SG contributions made on their behalf.

Basis of policy commitment

These measures contained within this Bill were announced in the Minister for Revenue and Assistant Treasurer's Press Release No. 003 of 19 January 2005 and Press Release No. 016 of 14 March 2005, following widespread consultation with business, the superannuation industry and consumer groups.[3]

Position of significant interest groups/press commentary

There has been little public reaction to these particular changes to the Choice regime.

Pros and cons

The proposed changes will streamline the introduction of the Choice regime from 1 July 2005. There are advantages and disadvantages to particular measures. These will be discussed in the Main Provisions section below.

ALP/Australian Democrat/Greens policy position/commitments

The opposition has not made any comments on these particular measures to date.

Main Provisions

SHASA

Item 1 of Schedule 1 amends the *Small Superannuation Accounts Act 1995* to effectively close the 'Superannuation Holding Accounts Special Account (SHASA)', administered by the Australian Tax Office (ATO), to new deposits from 1 July 2006.

What is SHASA?

SHASA acts as a place where SG contributions, that cannot be made to an employee's fund, may be paid by an employer in satisfaction of that employer's obligation under the Superannuation Guarantee regime. For example, a person may work, say as a fruit picker, and suddenly leave that employer without providing a forwarding address or details of where to pay their SG entitlements. In these circumstances an employer could pay the employee's SG entitlements into SHASA.

SHASA pays no interest, and does not charge any fees. The ATO is required to try and make regular efforts to contact individuals with monies in SHASA and arrange for these monies to be transferred into superannuation funds that pay a rate of return (and also charge a fee).

Why Close SHASA?

In his Second Reading Speech the Minister for Revenue and Assistant Treasurer noted that:

> The Superannuation Holding Account Special Account was originally established to receive small superannuation amounts from employers who cannot find a superannuation fund. This facility is no longer needed, as Retirement Savings Accounts (RSAs) offer similar low-cost benefits for employers.[4]

What are RSAs?

Retirement Savings Accounts are superannuation accounts operated by banks and other financial institutions. They may be thought of as bank accounts that operate within the superannuation environment.

Are RSAs low cost?

It is not clear that RSAs are low cost accounts. In the year to 30 June 2004 the reported total expenses of RSAs were about 2.3 per cent of assets under management This is high compared with an average fees and expenses of about 1.29 per cent of assets under management across the entire superannuation industry in the same year.[5] Further, exit fees may also apply.[6]

Such fees would be acceptable if the investment performance of RSA was high. As at 11 March 2005 stated rates of return on the Commonwealth Bank's RSA were between 2.95 and 5 per cent per annum, depending on the balance in the account.[7] Generally, these rates of return are far less than those achieved by other investment entities in the superannuation environment.

As amounts going into RSAs in these circumstances are likely to be comparatively small it is more than likely that the rate of return on such accounts will be towards the lower end of this range.

Item 7 of Schedule 1 amends the SG Act to allow an account under section 8 of the *Small Superannuation Accounts Act 1995* to be an eligible choice fund for Choice regime purposes, but only before 1 July 2006.

Employer Charging Fees for Choice

Item 6 of Schedule 1 specifies that if an employer imposes a direct cost or charge on the employee as a consequence of having to contribute to the employees chosen fund – then that contribution is taken not to satisfy the requirements of the Choice regime.

As previously noted, the penalty for not meeting the Choice regime's requirements is capped at $500 per employee per notice period. The Commissioner for Taxation has the option of reducing this penalty by any appropriate amount, including to nil.[8] Under section 21 of the SG Act the Commissioner must make available, on the internet, guidelines governing the reduction of penalties under the Choice regime.[9] Whether these penalties are effective in deterring such behaviour remains to be seen.

Choosing a Fund Before 1 July 2005

Item 9 of Schedule 1 amends the SG Act to allow any fund chosen in conformity with the Choice regime before 1 July 2005 to be that employee's chosen fund from 1 July 2005, or two months after the choice was made, whichever occurs later.

This allows employees who commenced work with an employer before 1 July 2005 to choose a fund. They do not have to be offered the choice of fund after 1 July 2005 (see **Item 11 Schedule 1,** proposed new section 32NA(3) in the SG Act). Nothing in this Bill, or the other provisions of the Choice regime, prevents such employees from making another choice of fund after 12 months have elapsed.

Giving Additional Choice Forms

Item 10 of Schedule 1 simply allows the employer to give the employee a new Choice form if, after they had given the first form, discover they cannot in fact contribute to the default fund specified on the first choice form.

The updated choice form must be given within 28 days of an employer first becoming aware that they cannot contribute to the default fund specified on the first choice form.

Exclusion from the Choice regime

As noted above, participation in the Choice regime is done via the filling out of the prescribed Choice form. Under Section 32N of the SG Act an employer must give an employee a Choice form:

- within 28 days from 1 July 2005
- within 28 days of an employee's written request to do so
- within 28 days of an employer becoming aware of an employee's chosen fund ceasing to be their chosen fund due to the employer's inability to contribute to that fund or the

fund ceasing to satisfy the requirements to be an 'eligible choice fund' under section 32D or the SG Act, and

- within 28 days of the employer changing the fund to which they are making contributions on behalf of the employee.

The following amendments more precisely define circumstances where the prescribed Choice form does not have to be provided. In the following comments the description of the proposed amendments are indented and in bold text and the discussion of each provision (if any) is in normal text.

Item 11 of Schedule 1 also amends the SG Act to clarify circumstances where a Choice form need not be offered to:

> **to members an unfunded public sector superannuation scheme who are not Commonwealth employees(where those Commonwealth employees are members of the Commonwealth Superannuation Scheme (CSS) or Public Sector Superannuation Scheme (PSS)) (proposed subsection 32NA(4) of the SG Act)**

Under section 61 of the SG Act, an unfunded public sector scheme is a defined benefit superannuation scheme in respect of which:

- no fund has been established, and
- all or some of the amounts that will be required for the payment of the benefits are not paid into any fund established of the purposes of that scheme, or
- are not paid until the members become entitled to receive the benefits.

Effectively, this provision excludes members in unfunded state government superannuation schemes from participating in the Choice regime.

Commonwealth employees who are not members of either the PSS or CSS will be offered the Choice of superannuation fund from 1 July 2006, at the latest.

> **a person who ceases to be an employee before the end of the period for giving the standard choice form to that employee (proposed subsection 32NA(5) of the SG Act)**

As noted above, the period for giving the Choice form to an employee is 28 days after various events take place.

> **where it was a condition of employment that the employee choose a superannuation fund, and they have not done so and the employer does not have an arrangement to make SG payments into a superannuation fund on the behalf of that employee (proposed subsection 32NA(6) of the SG Act)**

> **where the employee is a member of the employer's defined benefit fund, and that fund is in surplus (proposed subsection 32NA(7) of the SG Act)**

When a defined benefit fund[10] is in surplus it has enough accumulated assets to pay all of its expected liabilities. In these circumstances employers are often not making contributions to such funds on behalf of there employees, as their superannuation obligations have been satisfied. Subsection 20(2) of the SG Act defines when a defined benefit fund is in surplus.

This provision prevents employees in these circumstances having additional superannuation contributions made on their behalf to another fund.

where the employee is a member of an employer's defined benefit fund and is entitled to their maximum benefit from that fund (proposed subsection 32NA(8) of the SG Act)

If a member of a defined benefit fund's superannuation benefit will not increase other than by:

- increases in salary
- investment earnings
- indexation according to a price index, or
- in other ways prescribed for the purposes of this paragraph.

then for Choice purposes they have achieved their maximum benefit (see subsection 20(3) SG Act).

For example, a person who has been a member of the Commonwealth Superannuation Scheme (CSS) for 40 years will not increase their benefits other than by an increase in wages and/or investment earnings. Further time spent working for the Commonwealth will not increase their benefits.

Again, this provision prevents the additional payment of superannuation contributions to another superannuation fund in these circumstances.

where a defined benefit fund member was entitled to a benefit whether or not SG contributions were made on their behalf to that defined benefit scheme.

This provision, again, prevents contributions being made on the behalf of an employee when the employer is already funding their superannuation benefits through a defined benefit arrangement. It prevents the potential double payment of superannuation benefits by employers.

The above exclusions from providing a Choice form largely clarify the exclusions that already existed in the SG Act.

ASIC to Enforce Particular Sections of the SIS Act

Items 12 to 14 of Schedule 1 amend the *Superannuation Industry (Supervision) Act 1993* (SIS Act) so that the responsibility for enforcing section 68A of that Act rests with the Australian Securities and Investments Commission (ASIC). Currently the Australian Prudential Regulation Authority has responsibility for this particular section of the SIS Act.

Section 68A of the SIS Act prohibits superannuation fund trustees from supplying goods or services to an employer or other person on condition that one or more employees of that person become members of that superannuation fund.[11] ASIC has been quite active in the prosecution of financial and securities offences.

Retirement Savings Account Act

Items 1 and 2 of Schedule 2 amend the *Retirement Savings Account Act 1997*. The proposed changes allow for the supply of some goods and services to employers or others allowed in regulations. These provisions are similar to those already existing in subsection 68A(4) of the SIS Act.

Concluding Comments

The response to the Choice regime is the most important issue currently facing the superannuation industry.

The major issue arising from the proposed amendments is the use of RSAs. As previously noted, generally small amounts will flow into RSAs as a result of the closure of SHASA. If the rate of return of these accounts is only about 2.95 per cent, and the cost of operating that account is 2.3 per cent a year, after inflation is considered, the value of these accounts in real terms will decline over time.

The Government has also indicated that it would amend the Choice legislation to extend the Choice regime to persons employed under State Industrial Awards from 1 July 2006.[12]

Endnotes

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1 Section 32F *Superannuation Guarantee (Administration) Act 1992.*

2 Section 32C *Superannuation Guarantee (Administration) Act 1992.*

3 The Hon. Mal Brough MP, Minister for Revenue and Assistant Treasurer, *Superannuation Choice – A Smooth Transition for Business and Employees*, Press Release, No 003,19 January 2005 at http://assistant.treasurer.gov.au/mtb/content/pressreleases/2005/003.asp accessed 30

May 2005 and, *Full Steam Ahead to Super Choice on 1 July*, Press Release, No 16 of 14 March 2005 at http://assistant.treasurer.gov.au/mtb/content/pressreleases/2005/016.asp accessed 30 May 2005.

4 The Hon. Mal Brough MP, Minister for Revenue and Assistant Treasurer, 'Second reading speech: Superannuation Legislation Amendment (Choice of Superannuation Fund) Bill 2005, House of Representatives', *Debates*, 26 May 2005, p. 10.

5 RiceWalker Actuaries, *Superannuation Fees and Expenses - Market Segment Analysis*, March 2005, p. 5.

6 Australian Taxation Office, Fact Sheet, *Retirement savings accounts and your superannuation*, 2 July 2004 at http://www.ato.gov.au/super/content.asp?doc=/content/19138.htm&page=7&H7 accessed 30 May 2005.

7 Commonwealth Bank RSA Standard Rate Component for RSA, effective 11 March 2005 at http://www.commbank.com.au/personal/other/rates_and_fees/investment.asp#RetirementSavingsAccountRates accessed 30 May 2005.

8 Subsection 19(2E) *Superannuation Guarantee (Administration) Act 1992*.

9 However, the following notes were found on the ATO's SuperChoice website. "During this period, an employer who demonstrates they have made a genuine effort to comply with the choice requirements will generally have any choice shortfall reduced to nil. However, penalties will not be reduced where the employer has not made any attempt to comply with the requirements of the law. These decisions will be made on a case-by-case basis." At http://www.superchoice.gov.au/employers/penalties/ accessed 30 May 2005.

10 Generally, a defined benefit fund is one where the member's final benefit is calculated with reference to a combination of their length of service, final salary, or both, or some other way not related to contributions and their associated investment earnings.

11 Some narrow exemptions to the provisions to section 68A SIS Act have already been made, see Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 1) at http://www.frli.gov.au/ComLaw/Legislation/LegislativeInstrument1.nsf/0/EA9CCE1EA0DF6316CA256FC3007E7394/$file/0413043B-050307EV.pdf accessed 30 May 2005.

12 The Hon. Mal Brough MP, Minister for Revenue and Assistant Treasurer, *Full Steam Ahead to Super Choice on 1 July*, Press Release, No 16, 14 March 2005 at http://assistant.treasurer.gov.au/mtb/content/pressreleases/2005/016.asp accessed 30 May 2005.

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