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RESEARCH PAPER NO. 3, 2010–11 9 September 2010

Superannuation 2010–2011

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Executive summary

This paper, updated for the 2010–11 financial year, is designed to provide readers with a summary of superannuation taxation, contribution, preservation and payment rules, and covers amongst others, the following topics:

- the taxation of superannuation contributions and benefits
- the level of superannuation contributions that employers must make (Superannuation Guarantee) (SG)
- the ability of superannuation fund members to direct contributions and benefits to different funds, such as choosing the destination fund for the SG contributions made on their behalf (Choice rules)
- the government co-contributions scheme for low income earners
- the ability to split superannuation contributions with a person's spouse
- taxation of superannuation fund income
- the preservation rules that came into operation on 1 July 1999
- the application of the goods and services tax (GST) to superannuation, and
- self managed superannuation funds.

ISSN 1834-9854

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Acknowledgements

Thanks to Ms Catherine Lorimer of the Parliamentary Library and staff from a major public service department for their comments and assistance. That said, any inaccuracies remain the responsibility of the author.

List of acronyms

ABN	Australian Business Number
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
AWOTE	Average Weekly Ordinary Time Earnings
GST	Goods and Services Tax
ITAA1936	*Income Tax Assessment Act 1936*
ITAA1997	*Income Tax Assessment Act 1997*
RSA	Retirement Savings Account
SG	Superannuation Guarantee
SG Act	*Superannuation Guarantee (Administration) Act 1992*
SGC	Superannuation Guarantee Charge
SIS Act	*Superannuation Industry (Supervision) Act 1993*
SIS Regs	Superannuation Industry (Supervision) Regulations 1994
SMSF	Self Managed Superannuation Fund
TFN	Tax File Number
TMC	Terminal Medical Condition

Introduction

General notes and disclaimer

In this paper, all figures in bold type are thresholds indexed in accordance with legislation governing the amounts that apply in a financial year and are only current for the 2010–11 financial year. This document will be updated at the beginning of every financial year.

Superannuation law is detailed and comprehensive, and individual circumstances can drastically alter its general application. This paper has been prepared as a briefing and reference tool only and is not intended for use in providing financial advice. This paper should not be used for determining the tax liability attached to superannuation benefits in any particular case, especially in view of the limited number of considerations that are addressed in a summary document of this kind. Nor should it be used to make any decision on the level of contributions to make to a superannuation fund or any decision on the choice of any superannuation fund.

The author, and those who have provided comments on this paper, disclaim any liability in relation to any financial decision taken which may be influenced by the content of this paper.

Australia's retirement income system

Australia's retirement income system is based on the so called 'three pillars':

1. compulsory superannuation contributions for all employees under the superannuation guarantee regime

2. voluntary superannuation contributions encouraged by tax concessions, and

3. a means tested social security age pension.[1]

This paper concentrates on the first two pillars, compulsory and voluntary superannuation contributions, and the payment of benefits from these sources for the year 2010–11.

Roles of various agencies

This document does not address the roles of the various government agencies that regulate the superannuation industry. However, it should be noted that taxation legislation and regulations administered by the Australian Taxation Office (ATO) are directed at superannuation funds and their members to collect revenue for the Commonwealth of Australia. The ATO also administers the co-contributions, superannuation guarantee and choice regimes and regulates self managed superannuation funds (SMSFs). Prudential legislation and regulations administered by the Australian Prudential Regulation Authority (APRA) (except in relation to SMSFs) are directed at safeguarding the assets of superannuation fund members and investors. Disclosure legislation and regulations administered by the Australian Securities and Investments Commission (ASIC) are directed at ensuring that fund trustees provide relevant information to superannuation fund members to help them make informed decisions. The Australian Transaction Reports and Analysis Centre (AUSTRAC) also regulates superannuation funds in regard to their identification of members and reporting of any suspicious transactions.

Superannuation contributions

This section explains how superannuation contributions are taxed, limits on the level of contributions that can be made to a superannuation fund without incurring additional tax and the tax offsets that apply to certain superannuation contributions.[2]

- A 'superannuation contribution' is a payment to a superannuation fund which, if made by an employer, is generally concessionally taxed.
- A 'tax offset' is a reduction in tax liability that has the same value to all taxpayers independent of the taxpayer's marginal tax rate.

Acceptance of contributions

- From 1 July 2007, a superannuation fund must not accept a member's contribution unless the member's tax file number (TFN) has been quoted to the fund's trustee. Contributions by a person that has not quoted their TFN to the fund trustee must be returned to the contributor within 30 days of the contribution being made.[3] A fund may still accept an employer's contribution made on the behalf of a member where the member's TFN has not been quoted but the fund will be subject to additional tax unless the TFN has been quoted by the end of the financial year. Some relief from this requirement is available in limited circumstances.[4]

Taxation of contributions

Generally, contributions to superannuation funds can be made in either one of two ways:

- before tax contributions that are tax deductible to the payer (who can be an employer or a self-employed fund member). They are known as tax deductible or concessional contributions, and
- after tax contributions that are not tax deductible to the payer (called non-deductible, non-concessional, un-deducted or personal contributions).

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1. Australian government, Treasury, *A Plan to Simplify and Streamline Superannuation - Detailed Outline*, May 2006, p. 1.
2. 'Tax offsets' is the generic term used by the Australian Taxation Office to refer to tax offsets, tax rebates and tax credits.
3. Superannuation Supervision (Industry) Regulations 1994 (SIS Regs), regulations 7.04(2) & (4).
4. Superannuation Industry (Supervision) Modification Declaration No 3 of 2007, applies only in relation to government co-contribution payments.

Tax deductible contributions are included in the assessable income of complying superannuation funds and retirement saving accounts (RSA). Complying funds and retirement savings accounts are taxed at a rate of 15 per cent.

In some circumstances, some of the tax paid on contributions may be claimed back on the death of a member (see Death Benefits below).

Generally, the personal superannuation contributions which an employee (or the self-employed) may make out of his or her after tax income are not eligible for a tax deduction and are not included in the income of complying superannuation funds or retirement saving accounts and are not subject to tax on entry into a fund.

See following sections for limits on contributions and tax applying to amounts over these limits.

Surcharge on contributions

With the passing of the *Superannuation Laws Amendment (Abolition of Surcharge) Act 2005* the superannuation contributions surcharge ceased to apply on tax deductible (or concessional) contributions made after 30 June 2005. However, the surcharge will continue to be paid by two groups:

- those who made surchargeable contributions or who had surchargeable contributions made on their behalf between 1996–97 and 2004–05 and their superannuation fund has not yet paid the relevant surcharge on their behalf, and
- unfunded defined benefit fund members who are liable to pay the surcharge for the years between 1996–97 and 2004–05, when they take their benefit (if they have not paid their liability out of other funds at an earlier point).
- A funded defined benefit scheme that received surchargeable contributions must pay the surcharge if they have not already done so.[5]

No further surcharge is payable by the first group after the outstanding surcharge amounts have been paid.

Members of defined benefit funds, who are liable to pay the surcharge, do not pay it in the year in which the liability arises. Rather, the notional liability is calculated and kept as a charge against their superannuation benefits, when they are eventually paid. Defined benefit fund members are also able to pay out their liability before the benefit is paid in order to reduce or avoid the interest that accrues on their surcharge liability.

5. A funded defined benefit fund is one where the benefits are fully backed by the asset of the scheme. An unfunded defined benefit fund is one where the benefit payable by the scheme is not full backed by the assets of the scheme.

Tax offset for superannuation contributions made for a low income spouse

A person is entitled to receive an 18 per cent rebate for contributions made to the superannuation fund or retirement savings account of their spouse (up to a maximum of $3000 in contributions per annum), provided the spouse has an assessable income plus reportable fringe benefits and reportable superannuation contributions of $10 800 or less per annum. The spouse must be under 65 years of age in the week in which the contribution was made. The maximum rebate of $540 phases out on a dollar-for-dollar basis and is not available when the low income spouse's assessable income plus reportable fringe benefits is $13 800 or more per annum.[6]

Contributions splitting

The superannuation contributions splitting rules allow a person to request the transfer of up to 85 per cent of tax deductible contributions made by their employer on their behalf and 100 per cent of their personal contributions, made in the previous financial year, to a superannuation account in their spouse's name.[7] Superannuation contributions able to be split between spouses are known as 'splittable contributions'. The following specific rules apply. For contributions made between 1 January 2006 and 30 June 2007, the following is the maximum amount of contributions that can be split in a year:

- 85 per cent of the taxed splittable contributions
- 100 per cent of untaxed splittable contributions (This will not include contributions made after 5 April 2007 to a superannuation fund or after 30 April 2007 to an RSA), and
- 100 per cent of untaxed splittable employer contributions.

For contributions made on `and after 1 July 2007, the following is the maximum amount of contributions a member can split in a financial year. For taxed splittable contributions, the lesser of:

- 85 per cent of the concessional contributions
- the concessional contributions cap for that year, and
- for untaxed splittable employer contributions, 100 per cent of the concessional contributions cap for that financial year.

As a result of changes to the contributions splitting laws no contributions made to a superannuation fund after 5 April 2007, or to an RSA after 30 April 2007, will be included in untaxed splittable contributions.

6. Income Tax Assessment Act 1997 (ITAA1997), s. 290–230.
7. SIS Regs, regulation 6.41(1) & (2).

The limit of 85 per cent on the amount of taxed splittable contributions is to ensure that members cannot split more than the amount remaining in their superannuation fund after taking into account the 15 per cent tax that could apply to those contributions.

A superannuation fund trustee can refuse to action these requests. From April 2007, members are no longer able to split untaxed contributions made on or after 5 April 2007.[8]

Proposed low income earners superannuation contribution tax rebate

Low income earners currently receive little, if any, tax benefit from superannuation. Those with incomes of less than $37 000 per annum are subject to a 15 per cent marginal tax rate, while those on incomes of less than $16 000 per annum do not pay any income tax. The Superannuation Fund Income Tax (applying to both tax deductible contributions and investment earnings) is also set at 15 per cent. In these circumstances there is no tax benefit to be gained by a low income earner having tax deductible contributions (known as concessional contributions) made on their behalf (such as SG contributions), or by making personal contributions.

From 1 July 2012, the government proposes to introduce a tax rebate of up to $500 per annum, in respect of concessional contributions made by individuals whose adjusted taxable incomes are less than $37 000 per annum. This threshold will not be indexed and the rebate will be paid directly into the individual's superannuation account.[9]

This proposed measure will affect all those with SG payments made on their behalf whose annual adjusted taxable income is less than $37 000 per annum.

Non-deductible or non-concessional contributions

Limits on contributions

As noted above, non-concessional contributions are contributions made by individuals on an after tax basis. From 1 July 2009 the following annual limits apply:

- **$150 000**, or
- those under age 65 can make contributions up to **$450 000** in non-concessional contributions over a three year period (which starts when more than $150 000 is contributed in a year).[10] If they make additional non-concessional contributions in that three year period over the **$450 000** limit the additional contributions are subject to a penalty rate of tax

8. SIS Regs, regulations 6.41(3) & (4).
9. Australian Government, *Budget measures: budget paper no. 2*, Commonwealth of Australia, Canberra, 2010, p. 40, viewed 12 May 2010, http://www.aph.gov.au/Budget/2010-11/content/bp2/download/bp2.pdf
10. ITAA1997, sections 292–20 & 290–85.

- those aged over 65 have to meet a work test (see below) in order to make non-concessional contributions of no more than **$150 000** per year. Those over age 65 do not qualify for the **$450 000** limit for these contributions over 3 years.

The $150 000 threshold is six times the concessional contributions threshold (see below).[11] The $450 000 limit is determined by it being three times the ordinary limit on non-concessional contributions (that is, $150 000). Beyond these annual limits, excess contributions tax may apply.

Both payments received for personal injury and certain small business CGT exempt amounts (see below) contributed to a superannuation fund are exempt from the above limits.[12]

Tax on excess non-concessional contributions

A tax of 46.5 per cent is imposed on the amount of a person's non-concessional contributions in excess of these annual limits.[13]

In circumstances where both concessional and non-concessional contributions are made during the one year, and both contributions caps are exceeded, the effective rate of tax on some contributions can be higher than the above mentioned rate.

In the case of an excessive non-concessional contributions tax liability, the member must take the required payment out of the super account.[14] They may then pay the tax liability with these funds.

Government superannuation co-contribution for low income earners

An employee for superannuation guarantee purposes, and the self-employed, may be entitled to a government superannuation co-contribution. Co-contributions do not count towards either contributions cap. These contributions are non-concessional contributions.

In the 2010–11 year of income, an employee with total annual total income less than **$31 920** who makes personal superannuation contributions is eligible for a matching $1 contribution from the government for every dollar of eligible personal contributions made to a complying superannuation fund.[15] The maximum amount of eligible personal contributions that the government will match is $1000. That is, the government will contribute $1000 if an employee with income less than **$31 920** makes $1000 or more in personal superannuation contributions.[16]

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11. ITAA1997, subsection 290–85(2).
12. ITAA1997, s. 292–90.
13. Superannuation (Excess Non-concessional Contributions Tax) Act 2007, sections 4 & 5, and ITAA1997, section 292–80.
14. ITAA1997, section 292–410.
15. 'Total income of a year of income' is defined in section 8 of the *Superannuation (Government Co-Contribution for Low Income Earners) Act 2003* as being the person's assessable income for the year of income, his or her reportable fringe benefits and superannuation contributions made by way of salary sacrifice, for the year of income.
16. The maximum rate of government contribution was $1.50 for every $1 contribution by the individual. However, legislative amendments in Schedule 2 of *Tax Laws Amendment (2009 Budget Measures Act No.1) 2009* changed this

As at the date of writing, after the 2011–12 financial year, government superannuation co-contribution rates will be as following:

- $1.25 for every $1 of eligible personal contribution in 2012–13 and 2013–14 years. That is, the maximum government superannuation co-contribution for these years will be $1250, and
- $1.50 for every $1 of eligible personal contribution in 2014–15 and later financial years. That is, the maximum annual government superannuation co-contribution will be $1500.[17]

In the 2010–11 year for an employee with a total income between **$31 920** and **$61 920**, the maximum amount of the government co-contribution is reduced by 3.333 cents for every dollar of annual earnings above **$31 920**.

The rate at which the above maximum government superannuation co-contribution is reduced, increases in later years, as follows:

- $0.04167 for every dollar that a person's annual income for co-contribution purposes exceeds the relevant lower threshold in 2012–2013 and 2013–2014, and
- $0.05 for every dollar that a person's income exceeds the relevant lower threshold in the 2014–15 year and later years.[18]

There is no entitlement to the co-contribution in the 2010–2011 year once an employee's total income is **$61 920** or more.[19] From the 2007–2008 year of income, these thresholds are indexed in line with full-time adult average weekly ordinary time earnings (but see below for proposed change). The following table sets out the levels of government co-contributions that may be paid, by total income and personal contributions made in the 2010–11 year of income.

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contribution rate to $1 for every $1 made in eligible personal contributions for the 2009–2010, 2010–2011 & 2011–2012 years only.

17. Changes made by Schedule 2 of Tax Laws Amendment (2009 Budget Measures Act No.1) 2009.
18. ibid.
19. Australian Taxation Office (ATO), *Key superannuation rates and thresholds*, 27 May 2010, viewed 31 May 2010, http://www.ato.gov.au/super/content.asp?doc=/content/60489.htm&page=20&H20

Table 1: Government Superannuation Co-contributions amount by income and personal contribution 2010–11

Total Personal Superannuation contribution(s) is	$1000	$800	$500	$200
Total Income for co-contributions purposes				
$31 920 or less	$1000	$800	$500	$200
$35 000	$897	$697	$397	$97
$40 000	$731	$531	$231	$20
$45 000	$564	$364	$64	$20
$50 000	$397	$197	$20	$20
$55 000	$231	$31	$20	$20
$60 000	$64	$20	$20	$20
$61 920	$0	$0	$0	$0

Source: Parliamentary Library[20]

The lowest amount of co-contribution payable is $20 per financial year. That is, if an employee contributes as little as $1 in personal contributions he or she will receive a co-contribution payment into their superannuation fund of at least $20 for the financial year.[21] In the above table, there are instances where the normal calculation for the 2010–2011 year to determine the amount of government superannuation co-contribution paid would result in no payment being made, despite more than $1 being contributed. In these circumstances the government will make a minimum payment of $20 into the person's superannuation account.

Changes in the definition of income for co-contributions purposes

For government superannuation co-contributions purposes, the definition of 'total income' is annual tax assessable income plus annual reportable fringe benefits plus superannuation contributions made by way of salary sacrifice.[22]

As noted above these contributions are non-deductible contributions. This means they are not subject to contributions tax. However, the investment earnings of the fund on co-contributions amounts are subject to tax (see below).

Proposed changes to the co-contribution regime

The government has proposed that these income thresholds will not increase for the 2010–11 and 2011–12 years only. Under the proposed change, these thresholds would next increase in the 2012–13 year.[23]

20. Author's estimations only in light of proposed changes in co-contributions regime.
21. Superannuation (Government Co-contributions for Low Income Earners) Act 2003, section 11.
22 ibid, subsection 8(1).
23. Australian Government, *Budget measures: budget paper no. 2*, op. cit., p. 299.

Further, the government proposes to make the current contribution rate of $1 for every $1 contributed by the individual (up to $1000 in personal contributions) a permanent feature of the co-contributions regime. The legislated changes in the superannuation co-contribution rate noted above will have to be repealed for this to occur.[24]

Contributions for children

A fund may accept contributions made 'in respect of a member who is under age 65'.[25] These contributions do not entitle the child's superannuation account to receive a government co-contribution payment, where that contribution has not arisen from the child's earned income.[26]

The work test

Amendments made to the Superannuation Industry (Supervision) Regulations 1994, with effect from 1 July 2004, allow anyone under 65 years of age to make contributions to a superannuation fund without needing to meet any work test requirements. From 1 July 2007 only those meeting the following requirements can make non-deductible contributions to a superannuation fund.

Between 65 and 75

A superannuation fund may accept contributions from a person in the following age groups:

- age 65 and over but not yet 70, if a person has been gainfully employed on at least a part time basis during the financial year in which the contributions are made (for example, personal contributions, spouse contributions)
- age 70 and over but not yet 75, only personal contributions (that is, no spouse contributions) if the person has been gainfully employed on at least a part time basis during the financial year in which the contributions were made.[27]

For the purposes of these particular rules, being 'gainfully employed on a part time basis' during a financial year requires the person to have worked at least 40 hours in a period of not more that 30 consecutive days in that financial year. For example, a person who works 40 hours in a fortnight can make superannuation contributions (within the above contribution limits) for the rest of the financial year.[28]

If a person aged between 65 and 75 continues to work but does not meet the 'gainfully employed on a part time basis' test their superannuation fund may still receive mandated employer contributions made on their behalf (that is, any award based contributions and superannuation guarantee contributions made by an employer, with the latter compulsorily payable up to age 70). The

24. ibid, p. 298.
25. SIS Regs, regulation 7.04(1).
26. Superannuation (Government Co-contribution for Low Income Earners) Act 2003, sections 6 and 8.
27. SIS Regs, regulation 7.04.
28. SIS Regs, regulation 7.01(3).

consequence of not meeting the work test within this age range is that the person themselves cannot make their own contributions to a superannuation fund.

Age 75 and over

If a person is aged 75 or more only mandated employer contributions (for example, award contributions) can be accepted on behalf of the person by a fund.[29]

Capital gains tax (CGT) exempt contributions

A person can contribute an amount arising from the sale of a small business to a superannuation fund without incurring either CGT or personal income tax liability provided relevant legislative requirements are met.[30] This money is called a 'CGT Exempt Component' and is also exempt from contributions tax when it is placed into a superannuation fund. These contributions will not count towards either contributions cap. [31]

The total of all CGT exempt amounts contributed to a superannuation fund in respect of an individual cannot exceed **$1 155 000** over that person's lifetime. This limit will be indexed in line with increases in the AWOTE rounded to the nearest multiple $5000.[32]

Additional requirements apply where the asset is held through a company or trust structure, or jointly held with another in a partnership arrangement.

Personal injury payments

Contributions arising from personal injury payments are exempt from the non-deductible contributions limits, if no tax deduction is claimed. The payment must be in the form of a 'structured settlement', an order for a personal injury payment, or lump sum workers compensation payment to be exempt from these limits.[33]

Tax deductible or concessional contributions

Limits on tax deductible or concessional contributions

From 1 July 2009, the following annual limits apply on concessional contributions made by an employer on behalf of an employee and by a self-employed individual claiming these contributions as a tax deduction against their taxable income:

29. SIS Regs, regulation 7.04. Under SIS Regs, regulation 5.01. Mandated employer contributions are contributions made by an employer for the benefit of a fund member that are superannuation guarantee contributions, superannuation guarantee shortfall components and award-related contributions or certain payments from the superannuation holding accounts special account.
30. ITAA1997, section 152–310.
31. ITAA1997,section 292–90.
32. ITAA1997, section 292–105 & 960–285.

- **$25 000** for the **2010–11** financial year (indexed), [34] or
- $50 000 for those aged 50 and over under special transitional arrangements
  - during the years 2009–10 to 2011–12 those over 50 years of age, in any of these financial years, will be able to have a total of $50 000 per annum contributed to a superannuation fund as salary sacrifice contributions and/or contributions made on their behalf by their employer. Such contributions will not attract the excess contributions tax (see below). This particular threshold is not indexed to annual movements in AWOTE. Employers can claim a tax deduction for amounts they contribute under these provisions.[35] There is no limit to the amount an employer can contribute but there will be additional tax imposed beyond the relevant limits.

Proposed change

From 1 July 2012, individuals aged 50 and over, with less than $500 000 in total superannuation benefits, may make up to $50 000 in annual concessional contributions, without being subject to excess contributions tax (see below).

The major differences from the current rules outlined above are:

- as noted above, the current $50 000 limit on concessional contributions for those aged 50 and over ends on 30 June 2012. The proposed change removes this time limit, and
- the proposed change limits the ability of a taxpayer aged over 50 years to make more than $25 000 in annual concessional contributions, if they already have more than $500 000 in superannuation benefits.[36]

Tax on excess concessional contributions

A tax of 31.5 per cent is imposed on the amount of a person's tax deductible contributions in excess of the above annual limits.[37] This tax is in addition to the 15 per cent contributions tax that may have already been paid on these excess contributions by the superannuation fund; bringing the total tax paid on excess contributions to 46.5 per cent (which is the top personal marginal tax rate plus Medicare levy).[38] Amounts of concessional contributions made in excess of these limits cannot be

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33. ITAA1997, section 292–95.
34. ATO, *Key superannuation rates and thresholds*, media release, Canberra, 18 March 2010, viewed 24 March 2010, http://ato.gov.au/superfunds/content.asp?doc=/content/60489.htm This threshold is the same as for the previous financial year, the increase in the Annual Weekly Ordinary Time Earnings (AWOTE) by which this threshold increases was not large enough to justify its increase for the 2010–2011 financial year.
35. Changes in Schedule 3 of *Tax Laws Amendment (2009 Budget Measures No. 1) Act 2009*. This particular threshold is not indexed.
36. Australian Government, *Budget measures: budget paper no. 2*, op. cit., p. 41.
37. Superannuation (Excess Concessional Contributions Tax) Act 2007, sections 4 & 5 and ITAA1997, section 292–15.
38. ATO, *Super contributions – too much super can mean extra tax*, webpage, 11 March 2010, viewed 24 March 2010, http://ato.gov.au/individuals/content.asp?doc=/content/00106372.htm&pc=001/002/064/002/003&mnu=42869&mfp=001/002&st=&cy=1&alias=supercaps

returned to the contributor to avoid this tax. A member may withdraw an amount equal to the tax liability to be paid and pay that liability with these amounts.[39]

In the case of an excess concessional contributions tax liability, the member has a choice of having all or some of the liability being released from their super account or they can simply pay the debt from other savings.

Concessional contributions by the self-employed

From 1 July 2007, the self-employed under the age of 75 can claim all personal superannuation contributions as a tax deduction, but the work test has to be satisfied if they are over age 65.[40] The unemployed aged under 65 also can claim personal contributions as a tax deduction, assuming of course they have the financial capacity to make such contributions and taxable income to offset the contributions against.

These contributions can be claimed as a tax deduction if less than 10 per cent of a person's assessable income and reportable fringe benefits are attributable to employment as an employee.[41]

Contributions that are not eligible for a tax deduction

Certain contributions are not eligible for a tax deduction. These contributions include:

- the roll-over of superannuation benefits
- a benefit transferred from an overseas superannuation fund[42]
- a directed termination payment paid into a superannuation plan by an employer under transitional arrangements that apply until 30 June 2012[43]
- a contribution made under the *Family Law Act 1975* to satisfy the entitlement of a former spouse (who may also be an employee)[44] and
- contributions paid in satisfaction of a superannuation guarantee charge obligation.[45]

Regulation of superannuation contributions—Industrial Awards and the Superannuation Guarantee

Tax deductible contributions are paid by an employer under an industrial award or by an employer under the provisions of the superannuation guarantee (SG) legislation or directly by a self-employed

39. ITAA1997, section 292–410.
40. ITAA1997, subsection 290–165(2).
41. ITAA1997, section 290–160.
42. ITAA1997, section 290–5.
43. *Income Tax (Transitional Provisions) Act 1997*, section 290-1.
44. ITAA1997, subsection 290–60(4).
45. ITAA1997, section 290–95.

individual. Employees can also arrange with their employer to have salary sacrifice contributions made on their behalf. Some employers also contribute more than the amount required by the SG provisions because they choose to do so.

Industrial awards

Details of the superannuation support that an employer is required to provide to employees can be prescribed under federal and state industrial awards in addition to the provisions of the Commonwealth's superannuation guarantee scheme. Section 139(1)(i) of the *Fair Work Act 2009* (FW Act) provides that terms about superannuation may be included in modern industrial awards. Modern awards came into effect from January 2010 (while other provisions of this Act commenced from 1 July 2009).

In its award modernisation decision of 19 December 2008, the Australian Industrial Relations Commission (AIRC) allowed the designation of one or more specifically named superannuation funds as default funds for the purposes of the choice of fund regime under the SG Act.46 The AIRC also allowed the continuation of any superannuation fund to which the employer was making contributions on behalf of employees as on 12 September 2008 to minimise inconvenience for employers and to facilitate current default fund arrangements. Standard superannuation clauses in modern awards include a model provision allowing any fund to which the employer was making contributions for the benefit of employees before 12 September 2008 as a default fund. Most industrial awards specify two or three industry superannuation funds or a superannuation fund relevant to the employees of a particular business, where those employees are a minority of those business' employees. [47]

It is important to note that the general requirement for employers to contribute 9 per cent of an employee's ordinary time earnings to a superannuation fund on the employee's behalf applies along industrial award provisions on minimum contributions.

The award based superannuation provisions may be replicated or modified in an enterprise agreement made under the FW Act, providing the agreement passes the 'Better Off Overall Test' in relation to a modern award. Thus, an agreement may make reference to an award superannuation provision, possibly at a higher employer contribution rate. State awards (with non corporate employers) will move to the national system over 2010. They will continue to operate for a year before terminating in 2011 under the *Fair Work State Referrals and Consequential Amendments Act 2009* which gives effect to referrals of industrial relations laws from most of the states to the Commonwealth.

46. Award Modernisation Decision — Request from the Minister for Employment and Workplace Relations 2008, AIRCFB 1000.
47. For example, see clause 35.4 of the Draft Manufacturing and Associated Industries and Occupations Award.

Superannuation guarantee scheme (SG)

The superannuation guarantee scheme requires all employers to provide a minimum of 9 per cent superannuation support in each financial year for employees (with limited exceptions).[48] From 1 July 2008, employers may only calculate the superannuation guarantee contributions with reference to an employee's ordinary time earnings.[49] The ordinary time earnings of an employee is the lesser of:

- the total of the employee's earnings in respect of ordinary hours of work and earnings consisting of over-award payments, shift loading and commission; but not including lump sum payments made on termination of employment in lieu of unused annual leave, long service leave or sick leave (in respect of the latter two terms within the meaning of the ITAA1997), or
- the maximum contribution base for the contribution period (see below).[50]

Ordinary time earnings

- On 13 May 2009 the ATO released a superannuation guarantee ruling that clarifies the meaning of 'ordinary time earnings'.[51] Under the ruling the concept of 'ordinary time earnings' would also include (amongst other payments):
- over award payments, where such payments were part of the employees ordinary hours of work (that is worked on a regular basis)
- shift loadings, in relation to the person's ordinary hours of work
- commissions
- allowances and loading in respect of a person's ordinary hours of work, such as site allowances, casual loading allowance, dirt allowances or a freezer allowance, but only in relation to the person's ordinary hours of work
- bonuses, in most cases
- piece rates
- paid leave
- payments in lieu of notice
- some workers compensation payments, and
- directors' fees.

48. Superannuation Guarantee (Administration) Act 1992 (SG Act), section 19.
49. SG Act, subsections 23(2)-23(5).
50 . SG Act, subsection 6(1).
51. ATO, Superannuation Guarantee Ruling SGR 2009/2 – *Superannuation guarantee: meaning of the terms 'ordinary time earnings' and 'salary or wages'*, Original Ruling, Canberra, 13 May 2009.

- However, certain payments are not included in a person’s ordinary time earnings for SG purposes. Amongst these payments are:
- overtime payments, and
- allowances which constitute a reimbursement of expenses.

Obligation to pay SG amounts

The requirement for an employer to pay SG amounts on behalf of their employees arises under the SG Act. The general operation of that Act is that all employers are liable for the Superannuation Guarantee Charge (SGC or the charge). The amount of the charge is reduced by the amount of SG contributions paid by the due date. If the employer does not make the required SG payments on behalf of their employees by the due date (28 days after the end of the relevant calendar year quarter) they are liable to pay the charge.[52] Relief from paying some elements of the charge is given if the SG payments are made within a further 28 day period.

If an employer refuses to provide a superannuation guarantee statement or additional information to enable the assessment of their SG obligations they may be required to pay double the required SG charge.[53]

Exemption from the superannuation guarantee charge

Following are the general circumstances where an employer is not liable to pay the SGC:

- when the employer makes the required SG payments by the due date
- when an employee is paid to do work of a domestic or private nature for not more than 30 hours a week
- where the employees’ superannuation arrangements are via a defined benefit superannuation fund, and the employee’s benefits are, at the time the SG contribution(s) are payable, fully funded[54]
  - a benefit is fully funded when the scheme holds enough assets to meet the payment of benefits for all of its members. The period during which this occurs and the employer is not required to make SG payments is known as a ‘superannuation contributions holiday’
- where the employee is paid less than $450 per month in salary/wages[55]
- where the employee is under 18 years of age and is employed part time(that is, less than 30 hours per week)[56]

52. SG Act, section 16.
53. SG Act, subsection 59(1).
54. SG Act, sections 22 and 23.
55. SG Act, section 27(2).

- where employees are temporarily working in Australia for an overseas employer and are covered by a bilateral social security agreement[57]
- where salary or wages are exempt from income tax under item 1.4 of the table in ITAA1997 section 51–5[58]
  - this exclusion refers to tax free wages and allowances earned by members of the military reserves during their reserve service, and
- a person who is over 70 years of age.[59]

The above list is not exhaustive but represents the major circumstances where an employer is not liable for the charge.

Proposed changes

The required SG contribution rate is proposed to rise from 9 to 12 per cent of ordinary time earnings in 2019–20. The proposed rise is gradual and will not commence until 2013–14, as shown in the following table:

Increases in the required SG contribution rate

Year	Rate (%)
2013–14	9.25
2014–15	9.50
2015–16	10.00
2016–17	10.50
2017–18	11.00
2018–19	11.50
2019–20	12.00

Source: Budget paper no. 2[60]

As noted above, currently employers are not obliged to make SG payments in respect of employees who are age 70 and over.[61] However, employers can make voluntary tax deductible superannuation contributions on behalf of employees between age 70 and 75, and the self-employed may make such contributions up until age 75.[62]

56. SG Act, section 28.
57. SG Act, subsection 27(1).
58. SG Act, section 28.
59. SG Act, section 27(1).
60. Australian Government, *Budget measures: budget paper no. 2*, op. cit., p. 42.
61. SG Act, section 27(1).
62. Australian Government, *Budget measures: budget paper no. 2*, op. cit., p. 44.

From 1 July 2013, the government proposes to raise the SG age limit from 70 to 75. This means that employers would be required to make SG contributions on behalf of workers in this age group. The self-employed will need to pass the work test for contributions to be accepted after they turn age 65.

Maximum contribution base

As noted above, employers who do not make superannuation guarantee contributions are liable for the SGC. The SGC is made up of the employer's superannuation guarantee shortfall (the amount that the employee should have received in superannuation guarantee contributions), an interest (or penalty) component and an administration component (to recover costs incurred by the ATO). When calculating an individual employee's superannuation guarantee shortfall, the amount of an employee's salary or wages used to calculate their 'ordinary time earnings' in a contribution period is limited to the maximum contribution base, which is **$42 220 per quarter** for the 2010–11 year.[63]

Quarterly superannuation guarantee

From 1 July 2003, employers have been required to make superannuation guarantee contributions on a quarterly basis.

Choice of superannuation fund

From 1 July 2005, most employees have been able to choose the complying superannuation fund into which they want to have their superannuation guarantee contributions paid. Where an employee does not choose a superannuation fund, the employer may choose the complying superannuation fund, provided it is an 'eligible choice fund'. An 'eligible choice fund' is:

- a complying superannuation fund
- a retirement savings account
- a fund presumed to be a complying superannuation scheme under section 24 of the SG Act, or
- a fund presumed to be a complying superannuation fund under section 25 of the SG Act.

However, the SG Act excludes various groups of employees from the coverage of the choice of superannuation fund legislation including:

- some employees who are members of defined benefit superannuation funds (principally in the public sector),
- employees under 'preserved' State Industrial Awards, and

63. ATO, Key superannuation rates and thresholds, 27 May 2010, op. cit.

- employees with superannuation entitlements under certain certified agreements or Australian Workplace Agreements.[64]

From 1 July 2006, choice of superannuation fund has applied to employees working for corporations that were previously under a State industrial award, but as a result of the *Workplace Relations Amendment (Work Choices) Act 2005* and associated regulations are now under the Federal workplace relations system.[65]

Portability

Briefly, portability allows superannuation fund members to transfer their superannuation fund balances to another superannuation account in their own name. Portability makes it easer to consolidate a person's multiple superannuation accounts.[66]

Australia and New Zealand have agreed in principle to allow movement of superannuation benefits between Australian and New Zealand superannuation funds. The final details of the scheme are currently under discussion. [67]

Taxation of superannuation fund earnings

The assessable income of a complying superannuation fund or retirement savings account, comprising of both the investment earnings and the contributions received, are generally taxed at a rate of 15 per cent. The capital gains tax discount for superannuation funds is one third of the capital gains included in a superannuation fund's assessable income.

The tax that a superannuation fund pays on its assessable income can be reduced through the use of imputation credits, the current pension income exemption, [68] and other deductions such as those related to property investment.[69] In practice the average rate of tax on the earnings of a superannuation fund is about 7.1 per cent per annum.[70]

Non-complying superannuation funds are taxed at a rate of 45 per cent on their assessable income, including realised capital gains and taxable contributions.[71] Superannuation funds can be non-complying either through choice or through failing to meet the necessary standards and conditions

64. SG Act, sections 32NA and 32C.
65. Workplace Relations Amendment (Work Choices) (Consequential Amendments) Regulations 2006 (No. 1), Schedule 17.This Schedule makes necessary amendments to the SIS Regs.
66. SIS Regs, Division 6.5.
67. Australian Government, *2009–10 Budget Paper No. 2*, p. 36.
68. A superannuation fund is not taxed on income it receives that is used to pay a pension.
69. Imputation credits form part of the dividend imputation system. *The Australian Financial Review: Dictionary of Investment Terms*, 5th edition, Sydney, 2000, p. 110, describes 'Imputation Credit' as taxation credits which are passed onto shareholders who have received franked dividends in relation to their shareholdings. Imputation credits arising from the company tax paid by a company in relation to its profits.
70. Australian Government, *International Comparison of Australia's Taxes*, Canberra, 3 April 2006, p. 229.
71. Income Tax Rates Act 1986, subsection 26(2).

required under prudential legislation to qualify for tax concessions. All APRA regulated and licensed funds are complying funds.

Payment and taxation of superannuation benefits

This section describes the taxation arrangements that apply to superannuation benefits. A superannuation benefit generally is the amount of money in the superannuation fund or retirement savings account to which the fund member or retirement savings account holder is entitled. Most benefits are in the form of lump sums or are capable of being converted into a lump sum. However, some schemes, including those covering many Commonwealth public servants, pay a substantial part of benefits in the form of a pension. Most benefits are payable to the member only on retirement or satisfaction of another condition of release, such as permanent disability, and will often be subject to preservation (see 'Preservation rules' below).

These amounts should not be confused with employment termination payments which refer to amounts paid arising solely from the termination of employment. This class of payments are not further discussed in this document.

Background

From 1 July 2007, a superannuation benefit may comprise the following:

- a tax free component
- a taxable component which may include
  - an element taxed in the fund, and/or
  - an element untaxed in the fund.

The tax free component of a superannuation benefit is generally made up of contributions from a person's post-tax income and by amounts which represent the portion of a superannuation benefit that accrued before 1 July 1983. The tax free component is exactly that—it is paid tax free; no matter whether it comes from a taxed or an untaxed source.

The taxable component of a superannuation benefit is the total value of the superannuation benefit *less* the tax free component. The tax treatment of a taxable component also depends on whether it is drawn from an element which has been taxed or untaxed in a fund. The taxed element of the taxable component is usually made up of tax deductible contributions made to the superannuation fund by the person and/or by the employer on the person's behalf, as well as earnings on all contributions. For most people the taxable component is entirely made up of an element taxed in the fund, that is, a part that has been subject to tax at the time that contributions were made and upon earnings.

Most members draw benefits from an element that has been taxed in a fund. In comparison, an element untaxed in the fund usually arises in public sector superannuation plans that are of the defined benefit type where tax has not been paid on contributions or earnings, or from unfunded schemes.[72] Only about 7 per cent of superannuation funds are of the defined benefit type.[73] An element untaxed in the fund can also be relevant when a taxed fund pays out a death benefit, including an insurance payout, to a non-dependant such as an adult child.

Different taxation arrangements apply to the element taxed in the fund and the element untaxed in the fund. These arrangements are summarised in the following tables. The tax rates specified in the tables are maximum rates of tax. The Medicare levy (1.5 per cent per annum) is also payable upon any superannuation benefit where a tax rate greater than zero per cent applies.[74]

Table 2: Tax treatment of superannuation member benefits -taxed elements

Age when benefit received	Superannuation lump sum	Superannuation pension
Aged 60 and above	Tax Free	Tax Free
Preservation age to 59	0% up to **$160 000**, 15% on amount above this figure	Marginal tax rate but with 15 % tax offset
Below preservation age	20%	Marginal tax rate but no tax offset for most pensions (a)

Source: Explanatory Memorandum to Simplified Super Legislation[75] and ATO, Key superannuation rates and thresholds for 2010–2011

(a) A disability superannuation pension received below preservation age receives a 15 % tax offset

The superannuation pension offset and preservation age are discussed further below.

The following table summarises the taxation treatment of the benefits that are untaxed in the fund. These rates apply from 1 July 2007. An additional Medicare levy of 1.5 per cent also applies.

72. An ‘unfunded’ scheme is one where the benefits are contributed to the scheme only when the member claims those benefits. That is, the benefits are not funded by either the employee or the employer during the time of that person’s membership.
73. Australian Prudential Regulatory Authority, ‘Statistics’, *Annual Superannuation Bulletin*, June 2008 (issued 10 March 2009), p. 42, and Australian Government, *A Plan to simplify and streamline superannuation – Detailed outline*, May 2006, p. 45.
74. Explanatory Memorandum, Tax Laws Amendment (Simplified Superannuation) Bill 2006, pp. 45 and following.
75. ibid.

Table 3: Tax treatment of superannuation member benefits -untaxed elements

Age when benefit received	Superannuation lump sum	Superannuation pension
Aged 60 and above	15% on first **$1.155m** per superannuation plan. Top marginal rate on amounts over this	Marginal tax rates and 10 per cent of gross pension paid tax offset
Preservation age to 59	15% on first **$160 000**, 30% on amounts between this figure and **$1.155m** and top marginal rate on amounts above **$1.155m**	Marginal tax rates but no tax offset
Below preservation age	30% on amounts up to **$1.155m**, top marginal rate thereafter	Marginal tax rates but no tax offset

Source: Explanatory Memorandum to Simplified Super Legislation[76] and ATO, Key superannuation rates and thresholds for 2010–2011

Terminal illness

- From 1 July 2007 tax free superannuation benefits may be paid to those suffering a terminal illness. The person may be below both their preservation age and age 60 when such a payment takes place.[77]

- The government has announced that it proposes to permit complying superannuation funds and retirement savings account providers to deduct terminal medical condition (TMC) benefits from their fund's taxable income. This proposal addresses an anomaly in the taxation law regarding deductibility by superannuation funds and RSA providers of the costs of providing certain benefits to members/holders. Current deductions are allowable of the cost of providing benefits relating to the death, permanent incapacity and temporary incapacity conditions of release, but not those relating to TMC conditions of release.[78]

Pension tax offsets

From 1 July 2007 there are two main tax offsets applying to recipients of superannuation pensions:

- a tax offset equal to 15 per cent of the pension arising from a taxed source[79] for recipients aged between preservation age (currently 55) and 59, and

- a tax offset equal to 10 per cent of the pension paid from an untaxed source where the recipient is 60 years of age or over.[80]

76. ibid.
77. Schedule 7 *Tax Laws Amendment (2008 Measures No. 2) Act 2008*, Schedule 7, and P Dutton, (then Minister for Finance and Assistant Treasurer), *Australians with terminal illness will now be able to draw super tax free*, media release, 11 September 2007.
78. Australian Government, *Budget measures: budget paper no. 2*, op. cit., p. 48. A condition or release is the circumstances under which a superannuation benefit can be paid out. These conditions are contained in the schedules to the SIS Regs.
79. ITAA1997, section 301–25.

- Some pensions, such as those paid from the Commonwealth's Public Sector Superannuation Scheme (PSS), may contain payments from both a taxed and an untaxed source, along with some tax free amounts representing return of the member's own after-tax contributions. These pensions would qualify for both of the above tax offsets on the relevant components, provided that the age requirements are met. It should also be noted that the portion from a taxed source becomes tax free at age 60.

No compulsory payout of superannuation benefits

A member is able to leave their benefits in their superannuation fund indefinitely. They are able to withdraw as much, or as little, as they choose at any time after their preservation age provided that they have met a condition or release.[81] The decision to leave benefits in a superannuation fund indefinitely is subject to the rules of the particular superannuation fund involved. However, investment earnings within the fund are tax free if the amount concerned is used to finance an income stream which meets the requirements of the legislation.

The ability to leave superannuation benefits in a fund indefinitely commenced on 10 May 2006.[82] The death of a member, however, is still a compulsory condition or release.

Payment of income streams (pensions)

From 20 September 2007, the following arrangements govern the payment of income streams from a superannuation fund:

- only the required payment of a minimum amount per year
- no upper limit on the annual amount paid (including cashing out the entire amount of capital backing the pension)
- no provision for an amount to be left over when the pension ceases, and
- the pension would be transferred only on the death of the recipient to their dependant(s), or cashed out as a lump sum to the dependant's estate. Such a pension cannot be paid to a child aged 25 and over unless the child is permanently disabled.[83]
- The following table illustrates the minimum annual pension payment rates, by age; applying from 20 September 2007.

80. ITAA1997, section 301–100.
81. Australian Government, Treasury, A Plan to Simplify and Streamline Superannuation – Detailed Outline, 9 May 2006, p. 20.
82. P Costello (then Treasurer), A plan to simplify and streamline superannuation – transitional issues that apply immediately, media release, No. 57 of 2006, 14 June 2006.
83. Australian Government, Treasury, A Plan to Simplify and Streamline Superannuation– Detailed Outline, 9 May 2006, p. 21.

Table 4: Required minimum superannuation pension payments

Age	Minimum payment percentage	Minimum annual payment for each $100 000 in the account
Under 65	4%	$4000
65–74	5%	$5000
75–79	6%	$6000
80–84	7%	$7000
85–89	9%	$9000
90–95	11%	$11 000
95 or more	14%	$14 000

Source: SIS Regs, Schedule 7.

Say a person, aged 56, elected to take their superannuation benefit in the form of a pension. Further, that the benefit was worth $100 000 when they made this decision. The minimum amount to be paid in that financial year would be $4000. The person could decide to take a larger pension in that financial year if they so wished.

Pension draw-down relief

On 18 February 2009, the Government suspended the minimum payment requirement for account-based pensions for the second half of 2008–09. This was achieved through a 50 per cent reduction in the minimum payment amounts that would otherwise apply for the 2008–09 financial year. Regulations were drawn up to implement this policy for the remainder of the 2008–2009 financial year.[84]

For example, a self-funded retiree who is 60 years of age would have been required during a year to draw a minimum annual pension payment of 4 per cent of their account balance as at 1 July. Under the new regulations, this percentage is reduced to 2 per cent for the 2008–2009 financial year.

This relief was extended to the 2010–2011 year (only) on 12 May 2009.[85]

Proportioning

Since 1 July 2007, both lump sum and account based pension[86] benefits paid from superannuation funds are divided into both taxed and tax free amounts. Partial payouts are also divided into these components, in the same proportion as the main benefit.[87] For example, if the main benefit was

84. N Sherry, (then Minister for Superannuation and Corporate Law), *Regulations released for pension drawdown measure to benefit retirees*, media release, No. 22, Canberra, 16 March 2009. Regulations are Superannuation Industry (Supervision) Amendment Regulations 2009 (No. 2).
85. W Swan (Treasurer), N Sherry (Assistant Treasurer), C Bowen (Minister for Human Services and Minister for Financial Services, Superannuation and Corporate Law), *Self funded retirees to benefit from extension in drawdown relief for account based pensions*, Joint media release, Canberra, 30 June 2010.
86. An account based pension is one based on a separate account within a superannuation fund held in the member's name.
87. ITAA1997, section 307–125.

made up of 30 per cent tax free and 70 per cent taxed components then any partial withdrawal would be similarly proportioned.

This rule does not impact on the payment of benefits from a fully taxed source if the recipient is aged 60 or more. As noted above, such benefits are tax free in the hands of the recipient. However, this rule affects partial withdrawals made before that age, such as withdrawals under financial hardship or on compassionate grounds, particularly where the benefit contains a significant amount of non-deductible contributions (that is contributions made on an after tax basis). This rule may also affect death benefits paid to non-dependents.

Preservation rules

'Preservation' refers to the prudential regulatory requirement that certain superannuation benefits be maintained either in a superannuation or rollover fund or retirement savings account until a condition of release is met.[88]

Preservation age

'Preservation age' is the age at which a fund member can gain access to benefits that have accumulated in a superannuation fund or retirement savings account, provided that the member has permanently retired from the workforce.

The government announced in the 1997 Budget that the preservation age would be increased from 55 to 60 years on a phased-in basis. By 2025, the preservation age will be 60 years for anyone born after 30 June 1964, with the preservation age being reduced by one year for each year that the person's birthday is before 1 July 1964. This means that persons born before 1 July 1960 will continue to have a preservation age of 55. The following table summarises the phase-in schedule:

Table 5: Preservation ages by date of birth

For a person born	Preservation age (years)
Before 1 July 1960	55
1 July 1960–30 June 1961	56
1 July 1961–30 June 1962	57
1 July 1962–30 June 1963	58
1 July 1963–30 June 1964	59
After 30 June 1964	60

Source: SIS Regs, regulation 6.01(2)

Prior to 1 July 1999, some monies held in a member's superannuation fund account were unpreserved benefits and could be accessed, subject to some restrictions, without having to wait

88. These prudential regulatory requirements are set out in the *SIS Act* and SIS Regs, regulations 6.18 and 6.19 and Part 1 of Schedule 1.

until the member had reached the preservation age and retired from the workforce. An example is non-deductible (or member) contributions made from after-tax income prior to 1 July 1999, where the member is no longer working for the employer with whom they were employed when he or she made these non-deductible contributions.

Preservation rules from 1 July 1999

The preservation rules changed significantly from 1 July 1999. These rules provided that all superannuation contributions (including member contributions) and superannuation fund investment earnings, from that date forward, would be preserved until the member's preservation age. Pre-1 July 1999, non-preserved components of a member's superannuation entitlement generally retain their non-preserved status.

From 1 July 2004, any employer eligible termination payment rolled over into a superannuation fund or approved deposit fund must be preserved until the member satisfies a condition of release that allows them access to their preserved benefits, such as retiring from the workforce once he or she has reached their preservation age. From 1 July 2007, the only employer termination payments that can be rolled into superannuation are those that were specified in existing employment contracts as at 9 May 2006 and are paid in before 1 July 2012.

Accessing superannuation before retirement

Preserved superannuation benefits can be accessed before preservation age on compassionate grounds and severe financial hardship or as the result of permanent incapacity. The rules and procedures in regard to release on compassionate grounds or financial hardship are strictly prescribed in the legislation.

Transition to retirement pensions

From 1 July 2005, a person who has reached their preservation age may access their superannuation benefits in the form of a non-commutable income stream without having to retire or leave their current employment. Further, pensions taken under these provisions can be stopped at any time and restarted at a later date.[89] These measures were designed to cater for more flexible working arrangements towards the end of a person's working life. These pensions are known as 'transition to retirement' pensions

89. Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 2) and Retirement Savings Accounts Amendment Regulations 2005 (No. 1). Any type of income stream can be taken under these provisions, including allocated pensions or market linked pensions. However, they are non-commutable until the person has reached 65 and retired.

For all new such pensions, no more than 10 per cent of the account balance of a transition to retirement pension can be withdrawn as a pension payment in any one year.[90]

Departing Australia superannuation payments

From 1 July 2002, temporary residents who permanently depart Australia can gain access to their accumulated superannuation. To be eligible for a payment:

- the person must have entered Australia on an eligible temporary resident visa (New Zealand residents are excluded)
- the person's visa must have expired or been cancelled, and
- the person must have permanently departed Australia.

The payment of superannuation benefits that qualify as Departing Australia Superannuation Payments are subject to special withholding tax rates to claw back the tax concessions the contributions received when originally paid into the superannuation. These rates are:

- tax free component – 0 per cent
- taxable component – 35 per cent, and
- untaxed component – 45 per cent.[91]

Future superannuation payments made on behalf of temporary residents (except those from New Zealand) will continue to be held by the relevant superannuation fund. However, if these benefits remain unclaimed 6 months after the departure of the former temporary resident these benefits will be paid to the Australian Government. Departed former temporary residents can then claim these benefits from the Australian Government (in practice the ATO) at any time.[92]

Death benefits

Lump sums

Briefly, lump sum superannuation benefits paid to a dependant of the deceased are tax free.[93]

If a non-dependant receives a lump sum benefit, and it includes a tax-free component, this amount remains tax free in the non-dependant's hands. Further, capped tax rates on the lump sum of 15 per cent for the taxed element and 30 per cent for the untaxed element apply.[94]

90. Australian Government, Treasury, A Plan to Simplify and Streamline Superannuation – Detailed Outline, 9 May 2006, p. 23.
91. Superannuation (Departing Australia Superannuation Payments Tax) Act 2007, section 5.
92. N Sherry (then Minister for Superannuation and Corporate Law), *Government announces new approach for temporary residents superannuation*, media release, No. 50. Gold Coast, 8 August 2008.
93. ITAA1997, section 302–60.

Pensions

Taxation of superannuation pensions paid as a result of the death of a member to their dependant is complex; depending on the age of the member on death, and the age of the person receiving it.

Since 1 July 2007, a non-dependant cannot receive a superannuation pension as a result of the death of a superannuation pensioner. A child aged 25 and over is generally regarded as a non-dependant. However, the non-dependant beneficiary in such circumstances may be entitled to receive a superannuation lump sum based on the commutation (that is cashing out) of a pension paid to the deceased.

Pensions that commenced to be paid to a person as a result of the death of a member before 1 July 2007 will continue to be paid. Where such pensions are paid to a non-dependant they are taxed as if they were received by a dependant.

The following table summarises the tax treatment of superannuation pensions paid to a non-dependant as the result of the death of a primary pension recipient.

Table 6: Tax treatment of superannuation pensions paid to a dependant of a deceased superannuation pensioner after 1 July 2007.

Age of the deceased at time of death	Age of the recipient	Tax Treatment of pension income in the hands of the non-dependant recipient
60 or above	Any age	Income arising from a taxable component – tax free Income arising from an untaxed component – marginal tax rates but with access to the 10% tax offset
Below age 60	Above age 60	Income arising from a taxable component – tax free Income arising from an untaxed component – marginal rates but with access to the 10% tax offset
Below age 60	Below age 60	Income arising from a taxable component – marginal tax rates but with access to the 15% tax offset Income arising from untaxed component – marginal tax rates (no access to the 10% tax offset).

Source: Explanatory Memorandum to Simplified Super Legislation[95]

Who is a dependant?

From 30 June 2004 the definition of 'dependant' was widened to include people living in an interdependent relationship.[96] An 'interdependent relationship' exists where the two people involved:

94. ITAA1997, sections 302–140 and 302–145.
95. Explanatory Memorandum, Tax Laws Amendment (Simplified Superannuation) Bill 2006, 7 December 2006, p. 49.
96. This includes people in a same-sex relationship where they meet the definition of an interdependent relationship.

- have a close personal relationship
- live together
- one or each of them provides the other with financial support, and
- one or each of them provides the other with domestic support and personal care.[97]

Same-sex couples

The above definition of an interdependent couple includes members of a same-sex couple. However, recent legislative changes enable the surviving member of a same-sex couple to be classed as a dependant for superannuation purposes without having to satisfy the requirements of the above interdependent relationship definition.[98]

Death benefits paid to non-dependants of the military and police serviceman

From 1 July 2007, payments made to non-dependants of Defence Force personal, Australian Protective Service officers and federal or state or territory police killed in the line of duty will be paid tax free.[99] Ex-gratia payments were made to those non-dependants who received superannuation payments between 1 January 1999 and 30 June 2007.[100]

Increased amount of death benefit payments

A death benefit lump sum, paid to a trustee of a deceased estate, spouse, former spouse or a child may be increased by part of the contributions tax paid on tax deductible contributions paid into the fund since 1 July 1988. The superannuation fund can recover any appropriate increase in the amount paid through a tax deduction.[101]

This applies only where the person dies as a member of a superannuation fund and where the trustees of the fund concerned agree to increase the death benefit payment. As noted above, due to the recent change in superannuation law a person may remain a member of a fund irrespective of age or attachment to the workforce, and withdraw as much or as little as they like. This may lead to increased numbers of persons remaining members of their superannuation fund until they die.

GST and superannuation

This section summarises how the GST is applied to superannuation funds.[102]

97. SIS Regs, regulation 10A, ITAA1997, section 302–200.
98. Same-sex *Relationships (Equal Treatment in Commonwealth Laws Superannuation)* Act *2008*.
99. ITAA1997, subsection 302–195(2).
100. Tax Laws Amendment (2007 Measures No. 3) Act 2007, Schedule 4, section 5.
101. ITAA1997, section 295–485.
102. For more details, see the Association of Superannuation Funds of Australia and the GST Start–Up Office, *The Goods and Services Tax and the Superannuation Industry Workbook, January 1999*.

The GST is a broad-based, value-added tax of 10 per cent on most goods and services supplied in Australia. It has been fully effective from 1 July 2000 (some contracts entered into before 1 July 2000 are also affected by the GST). The GST is payable on transactions where goods and/or services are supplied for consideration (payment). No business is necessarily GST-free; only certain transactions may be classified as such.

In all countries that have a GST-type tax, financial services are given special treatment. This is because of the difficulty in valuing the service provided when there are sums of capital and interest and other earnings in most financial transactions. It is difficult to determine GST on transactions comprising both a fee for service and an interest charge. Accordingly, financial services are 'input-taxed'.

Superannuation funds are in the business of making 'financial supplies', meaning that the provision, acquisition, or disposal of an interest in or under a superannuation fund, scheme, approved deposit fund or retirement savings account or in or under an annuity or allocated pension, is a financial supply.[103] Accordingly, no GST is payable by superannuation funds in respect of contributed capital and related fees paid by members or employer sponsors.

Most of the services provided to members by superannuation funds are free of GST; that is, they are 'input taxed financial supplies'. This means that superannuation funds pay GST on many of their purchases (such as computers), do not levy GST on the supplies they make to their ultimate customers (that is, on benefits paid to fund members), and are input-taxed (that is, they are not able to obtain input credit for the GST levied on the goods or services they purchased).

Nonetheless, in some circumstances superannuation funds are eligible for reduced input tax credits. For example, superannuation funds registered for GST purposes are eligible for reduced input taxed credits of the GST paid for administration and legal services. In addition, superannuation funds have to levy GST on their non-'input tax financial supplies', provided that the fund is registered or required to be registered for GST purposes. For example, superannuation funds are required to levy GST on the supply of premises to commercial property tenants. If a superannuation fund's turnover (which excludes input-taxed supplies) exceeds $75 000 per year, it must register with the ATO for GST purposes. The government is also encouraging people who manage their own superannuation funds to apply for an ABN to assist with the administration of their fund. Possession of an ABN does not necessarily mean that a superannuation fund is registered for the GST.[104]

Self managed superannuation funds

This section summarises the main features of a self managed superannuation fund (SMSF).

103. This is set out in regulation 40–13 of A New Tax System (Goods and Services Tax) Regulations 1999.

104. See The New Tax System Advisory Board, *Self Managed Super Funds Should Apply for an ABN Now*, media release, 28 May 2000.

General rules

An SMSF is a fund that:

- has a trust deed that meets the requirements of the *Superannuation Industry (Supervision) Act 1993* (Cth) (SIS Act)
- has no more than four members
- all the members are trustees of that fund
- the fund meets the normal residency requirements, that is it meets the definition of an Australian Superannuation Fund[105]
- no member of the fund is an employee of another member of the fund, unless they are related, and
- no trustee of the fund receives any remuneration for their services as trustee. [106]

Because all the members of an SMSF are trustees, the fund is not subject to the full range of prudential regulation and supervision. However, trustees of SMSFs still have to meet a number of obligations:

- lodging an annual income tax return and superannuation fund annual return
- lodging superannuation member contributions statements (MCS)
- reporting payments of member benefits
- appointing an approved auditor to complete the annual audit
- maintaining records for up to 10 years, and
- complying with investment restrictions.

Some of the SIS Act key compliance requirements applying to SMSFs include:

- meeting the sole purpose test
- formulating and giving effect to an investment strategy
- not releasing a member's money without the member meeting a specific condition of release
- not providing loans or financial assistance to members or relatives, and
- not borrowing money to invest (not withstanding the exception in section 67(4A) of the SIS Act relating to instalment warrants).

105. ITAA1997, subsection 295–95(2). .
106. SIS Act, section 17A.

SMSFs are regulated by the ATO.

Payment of pensions from an SMSF

An SMSF may pay an account based pension or a term allocated pension (sometimes called a 'market linked' pension) to its members.

However, there are restrictions on the ability of an SMSF to pay a defined benefit pension:

- if an SMSF was paying a defined benefit pension before 12 May 2004, or a specific entitlement to such a pension for a particular member of the fund existed before that date, it can continue to pay that pension or commence to pay that pension after 12 May 2004[107]
- under transitional rules, self managed superannuation funds can also pay a defined benefit pension to a person as long as:
  - the person was a member of the fund on 11 May 2004
  - before 1 January 2006, the person turns 65, or retires on or after turning 55
  - the person becomes entitled to the pension after 11 May 2004 and before 1 January 2006, and
  - the first pension payment is made within 12 months of the day the person became entitled to the pension [108]
- a SMSF cannot alter its trust deed/governing rules to allow for the payment of a defined benefit pension on or after 12 May 2004, and
- no SMSF established on or after 12 May 2004 may pay a defined benefit pension.[109]

107. SIS Regs regulation 9.041 and ATO Fact Sheet, *Self Managed Superannuation Funds and Pensions*, 31 May 2005.
108. M Brough, (then Minister for Revenue and Assistant Treasurer), *Extension of Transitional Arrangements for Small Funds*, media release, No. 049, 6 June 2005 and SIS Regs,regulation 9.041 and Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 4), which amends SIS Regs subregulaiton 9.041(3) to allow a SMSF to commence to pay a defined benefit pension in certain circumstances before 1 July 2006.
109. ATO Superannuation Determination, SD 2004/1, *Superannuation: can a self managed superannuation fund provide a defined benefit pension?*, viewed 16 June 2005, http://law.ato.gov.au/pdf/sd04-001.pdf, and M Brough (then Minister for Finance and Assistant Treasurer), *Outcome of the Review of Pensions in Small Superannuation funds*, media release, 27 September 2005.