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SELECT COMMITTEE ON SUPERANNUATION

Reference: Taxation treatment of transfers from overseas superannuation funds

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SENATE

SELECT COMMITTEE ON SUPERANNUATION AND FINANCIAL SERVICES

Wednesday, 22 May 2002

Members: Senator Watson *(Chair)*, Senator Sherry *(Deputy Chair)*, Senators Allison, Buckland, Chapman, Hogg and Lightfoot

Senators in attendance: Senators Allison, Buckland, Hogg and Watson

Terms of reference for the inquiry:

Taxation treatment of transfers from overseas superannuation funds

WITNESSES

ANDERSON, Dr Michaela, Director, Policy and Research, Association of Superannuation Funds of Australia 87

BARRETT, Ms Jane Margaret, Superannuation Policy Adviser, CPA Australia....101

ELLIS, Mr Paul Anthony, Principal, Human Capital, Andersen 121

FORSDICK, Mr Michael James, Partner, PricewaterhouseCoopers....112

GRIBBEN, Mr Anthony Charles Bernard (Private capacity) 65

HODGE, Mr Robert, Senior Policy Adviser (Tax), Association of Superannuation Funds of Australia....87

HUTTON, Mr Steven Brent, Director, Pension Transfers Direct Pty Ltd 127

KELLEHER, Ms Noelle Eileen, Member, Superannuation Centre of Excellence, CPA Australia.......101

MACKENZIE, Mr Gordon Donald, Senior Lecturer, ATAX, Faculty of Law, University of New South Wales 95

SKINNER, Mr Andrew Bryden, Vice-Chairman, Superannuation Committee, Taxation Institute of Australia 74

WHITELEY, Mr Phillip Martin (Private capacity) 134

Committee met at 9.03 a.m.

GRIBBEN, Mr Anthony Charles Bernard (Private capacity)

CHAIR—I declare open this hearing of Senate Select Committee on Superannuation. This is the second hearing that the committee has held as part of its inquiry into the way transfers from an overseas superannuation fund to an Australian regulated fund are taxed under section 27CAA of the Income Tax Assessment Act 1936. Superannuation is a form of long-term saving and investing which aims to provide income for people in their retirement. Tax concessions play a significant role in encouraging the saving for retirement through superannuation. However, these incentives are limited, and the tax laws feature a number of safeguards to ensure that the Commonwealth's revenues are not eroded by inappropriate access to tax concessions. Section 27CAA of the Income Tax Assessment Act 1936 is one such safeguard, which taxes the growth of a foreign superannuation benefit as the income of an Australian resident in certain circumstances. The purpose of this committee's inquiry is to explore whether the appropriate balance has been achieved or reached in the enhancement and administration of this particular provision.

Today we will be taking evidence from private individuals who are directly affected by the laws, such as Mr Anthony Gribben; superannuation industry organisations which represent the funds that are trustees of these important financial assets; professional advisers, firms and associations who advise on the tax consequences of transactions involving superannuation; as well as others who have an interest in these matters.

All of the witnesses who appear before the committee are protected by parliamentary privilege with respect to the evidence they give. This means that the witnesses are given a broad protection from action arising from what they say. The Senate has power to protect them from any action or any disadvantage on account of evidence given before the committee. The committee prefers to conduct its hearings in public; however, if there are any matters which you wish to discuss with the committee in private, we will consider your request. Today I welcome Mr Anthony Gribben. We have your submission. Would you like to comment on it? Following that we will ask you a number of questions.

Mr Gribben—Thank you. I am here in a private capacity. I migrated to Australia in 1993. As a result I am directly affected by the legislation. I think the legislation has good intentions to encourage current and future migrants to bring their pension funds to Australia when they come to Australia, or if they are already here to bring them over. However, I believe its implementation has been flawed and, in the case of existing migrants, has had the opposite effect—that is assuming that they know about the legislation, which is one of the major problems with the legislation. The primary flaw really is that the legislation has not been publicised. Those affected by it are generally unaware of it. Also, people tend to get their superannuation affairs in order later in life rather than earlier and people are eventually going to find out about this problem and by then they will have accumulated a large tax liability.

Also, the retrospective aspect of the law is not particularly fair given that most superannuation legislation seems to have grandfathered the changes so that current savings are not affected. The fact that it was enacted in 1994 and could go retrospectively back to however long somebody had already been in the country and had a super fund is unfair. The fact that the

transfer is taxed as income is inappropriate given that you cannot actually take the income because UK legislation, I believe, prevents this. It means that you can have a large income tax liability that is not easy for you to fund. In any case, it sort of defeats the point of bringing the super over if you are going to lose a large percentage of it. In my case I would lose about 25 per cent of my funds.

There is also too little time to affect the transfer. I can tell you from personal experience that Australian super funds are much more efficient than UK super funds. The idea that they could actually transfer money in six months is far too little time given that they also have their own prudential checks to make of the funds that people have to transfer to in Australia. I think the solution is that some way must be found to incentivise those people like me who have overseas funds to bring money to Australia rather than penalise them, which is how it seems to me at the moment. That will be a win-win for Australia in that it will bring more funds into the community, leading to more employment, less reliance by retirees on the state when they retire and more tax collected by the government in the long run. That concludes my statement.

CHAIR—You mention that the English super funds are not quite as efficient as the Australian. That is an interesting comment.

Mr Gribben—Here I get a statement from the super fund—say at the end of their year when they report the returns to you and how much the fees are and all that—within six weeks or two months. My super fund in the UK has an end-of-year of May and I am usually lucky if I have that statement by the following May. When I was living in the UK in the mid-1980s they introduced legislation enabling you to take your super from one employer to another. To make that transfer took 15 months. I know it was a long time ago, but my friends in the UK tell me that things have not improved very much. When I started talking to my company about bringing my pension fund here—before I knew about this legislation—the first thing you get told is, ‘I’m not sure you can do that.’ There is not a wide understanding of the law about transferring funds so it tends to go to the bottom of people’s in trays, and that is what takes the time, I believe.

CHAIR—You mentioned lack of knowledge. Is that lack of knowledge in Australia or in the UK?

Mr Gribben—To transfer funds?

CHAIR—Yes.

Mr Gribben—In Australia, there are two aspects to this. There is not a lot of knowledge about the legislation amongst those people whom it affects; generally they are unaware of it. In the UK as well they are generally surprised that you can transfer the money. They are more concerned about the day-to-day administration of the funds under UK law than worrying about what other countries might expect.

CHAIR—Are there any ways suggested to make communications better in order to better understand the products?

Mr Gribben—I had some correspondence with Senator Rod Kemp on this and I suggested that, in the migration packs that you can pick up around the world, people were made aware of

this law. He tacitly acknowledged that they do not do that by saying, ‘Yes, that is a good idea; we should do that.’ I suspect the only people who really know about the law are people who are in a similar position to me. I was a company transfer to Australia—they wanted me to move here and I wanted to move here so I got a migrant’s visa and migrated. They paid for me to go to a tax consultancy in the UK and get my affairs in order. Of course, it was in 1993 and this legislation was not in order then—they did not know about it—but I am sure that if I were there now they would know about this legislation and I would be able to handle my affairs. I am talking about a very small percentage of the people who migrate to Australia. They generally come more independently and they would not seek to get this advice.

CHAIR—An earlier witness indicated that there has been some misinformation from certain UK authorities on the operation—not pre-1983 but in relation to the current law.

Mr Gribben—When you say the UK authorities, do you mean the government?

CHAIR—No, the pension advisers.

Mr Gribben—Financial planners?

CHAIR—Yes.

Mr Gribben—I could believe that financial planners in the UK have different ideas of laws like that. I would not expect them to be across that sort of information. They have the same slightly mixed reputation that financial planners have here—that they are trying to sell you commissioned products and they are not really across all the issues.

CHAIR—Yes.

Mr Gribben—I do not live in the UK now, so it is very hard for me to comment about information coming out of the UK.

CHAIR—You made suggestions about the exemption period being extended to two years, lower tax rates at 15 per cent and improving awareness. These are issues that are common threads that have come through from most other witnesses. It is always good to hear from a person appearing before the committee in a private capacity because there is some personal feeling and meaning behind it, rather than necessarily a commercial advantage to the firm.

Mr Gribben—I personally feel wronged in that I would have been happy to comply with the law but I did not know about it. I suspect that there are a limited number of private submissions to the committee because there are a limited number of individuals who know about it. I would expect you would get more from the funds management people who seek to benefit from getting the money transferred in.

CHAIR—That is why we called you as a witness.

Senator HOGG—Where is your UK superannuation? Is it still in the UK?

Mr Gribben—Yes.

Senator HOGG—It is still there for the reason that if you were to bring it out here you would have a big tax bill.

Mr Gribben—I would get a big tax bill. It is about 25 per cent. I did mention the figures in the confidential attachment.

Senator HOGG—Yes. One of the things that is difficult for us to get a handle on is the real extent of the problem. I did not attend the first day of sitting because I had another commitment, unfortunately. I have read all the submissions to the inquiry and no-one seems to be able to pinpoint the extent. You said you raised the matter with your local MP, Mr Hockey, who in turn referred it to the Assistant Treasurer. When you were speaking with Mr Hockey, was he aware of other people who were in your circumstances?

Mr Gribben—He was and he actually named one well-known individual who he said always harangues him every time he sees him. It is John McFarlane of the ANZ Bank. He is Scottish and is in perhaps the same situation—although I do not know. He said he is always bending his ear whenever they are at functions about this legislation.

Senator HOGG—I was not specifically looking for other names. I was trying to get a feel as to whether or not you and maybe one or two others were isolated cases.

Mr Gribben—I know from personal experience about people who work at my company that I am not an isolated case. The other people affected by this legislation are younger than me and have tended to think that it is a problem that they will deal with later; their funds are also smaller. They are not actively pursuing transferring; they have taken the view that if they have to pay tax on it they will just leave it in the UK. It is very hard for me to comment generally on how big the problem is.

Senator HOGG—I accept that. I was looking more from your experience.

Mr Gribben—Joe Hockey said people had spoken to him about it but he said he had expected that because, at the time, he was the minister for finance and he had a good understanding of the legislation—he knew exactly what I was talking about; whereas Senator Kemp seems to take an obscure view of the legislation, saying that it was an affair for the tax commissioner because it was in law. He seemed to be missing the point that I was asking for the law to be changed.

Senator HOGG—That is the current Minister for the Arts and Sport. Do you have any intention of going back to the UK?

Mr Gribben—I have no intention but in today’s world I think you can never say, ‘Never.’ I have lived in Australia twice. I have got two young children and a wife here now and a home. I have got no real reason not to stay. My parents have died and there is no family connection in the UK any more. As far as I can see, I would be more than happy to live in Australia for the rest of my life but you do not know where your career might take you.

Senator HOGG—Given that your prospects of remaining in Australia are quite strong now and if there was a reasonable regime under which to bring your superannuation in—without disclosing the quantum of that, I would imagine that it would be a reasonable investment—would you be quite happy to see it invested in an Australian superannuation fund?

Mr Gribben—I said in the submission that I would definitely bring it in. I would not think twice about it. I was actually prepared to bring it in when I got round to thinking about in 1996, 1997, 1998. I did not know about the law at the time but when I knew that I would be taxed on the growth here and I knew that I could leave it in the UK and not be taxed, I was prepared to bring it in under those circumstances. You might have suggested that I would have been better off leaving it there because UK pension funds grow free of tax. The answer is: definitely, I would be very happy to bring it in.

Senator BUCKLAND—You mentioned that you would have to pay about 25 per cent on the funds that you take out and bring over as a lump sum?

Mr Gribben—Yes, that is an estimate.

Senator BUCKLAND—Do you have to contribute any money to maintain that fund as it is now?

Mr Gribben—No. The fund is frozen, if you like; it just grows and there are no contributions made to it.

Senator BUCKLAND—Take this scenario: in five years time when you find that you have made your fortune in Australia and you are going to stay here, to bring that money over then would you still have to pay that 25 per cent tax on it?

Mr Gribben—The 25 per cent is not the tax; it is the amount of the fund I would have to pay in tax. Because we hope the fund will continue to grow, potentially I will have to pay more, because I am not taxed on what the capital value was when I came here, which was about half its value now—I do not have a current up-to-date valuation.

Senator BUCKLAND—Are you taxed on the total as it stands at the time that you apply?

Mr Gribben—I am taxed on the difference between the value in May 1993 when I arrived in Australia and the value on the date I bring it in. So, assuming that the fund continues to grow, the tax liability continues to increase.

Senator HOGG—And it grows exponentially at that end so that in a sense you are further disadvantaged the longer you leave it. But of course you were unaware of the law.

Mr Gribben—Yes, that is right. I had five years where I did not know about the law and I had already accrued quite a tax liability. The fund's performance has not been as good in the last four or five years so the tax liability has not grown at the same rate, but it still continues to grow. It is a fairly substantial sum. As I say, I would have to take out a loan to pay the tax, which does not really seem a logical thing to do.

Senator BUCKLAND—If you were to return to the UK, could the superannuation you have now in Australia go with you?

Mr Gribben—I think it can if you go within 10 years, and I am at the nine-year anniversary now. So I think the effective answer is that I probably could not because I certainly have no plans to go back in the next year to live and after that it would be too late. There is also, of course, the opportunity for the UK government to change the law and say, 'You cannot bring your pension here.' That is a risk for Australia as well, in that it would make the legislation in place now fairly pointless. I would expect countries to make it harder for people to take money out.

Senator BUCKLAND—Have you spoken to tax consultants in Australia about this?

Mr Gribben—I have spoken to one or two people who should know.

Senator BUCKLAND—Are they professional tax consultants?

Mr Gribben—Yes, they are.

Senator BUCKLAND—Did they bring you to this idea of the two-year—

Mr Gribben—No, that was my idea.

Senator BUCKLAND—That was your own idea?

Mr Gribben—That is based on my personal experience dealing with UK pensions. Maybe you would consider two years too generous, but six months is certainly too short. You also have to think about the fact that when people migrate to a country they have many more things to worry about than bringing their superannuation fund with them, especially if they have a family or something.

Senator BUCKLAND—I would never dispute that, but in my view it is one of those issues that should be considered.

Mr Gribben—I agree.

Senator BUCKLAND—And it generally is not. It is one of the many things we do not think of until we are there.

Mr Gribben—It would actually be much easier to initiate a transfer in your last few weeks there because you could talk to the people directly, face-to-face or whatever. Although email is pretty good it is still only email; it is not like someone standing in the office, saying, 'I demand some action now.'

Senator BUCKLAND—You made a very important comment earlier on, in my view, where you said that because you came as a company transfer your company sent you to a tax consultant for professional advice. You are right that the majority of people who have come—the majority I have dealt with over the years—have come because they have made a family

e majority I have dealt with over the years—have come because they have made a family decision to come. Do you think in foreign countries where migration to Australia can take place freely that that information should be in an information kit that goes to intending migrants?

Mr Gribben—I think it should be and I think Senator Kemp made a tacit admission that it should.

Senator BUCKLAND—Yes, he did. But it is one of those things that would be tagged on at the end somewhere—do not forget your super; do not forget to pay the milkman before you leave.

Mr Gribben—I agree, but at least it might raise awareness. It is a bit like when you sign a contract to borrow some money or something and you then go and pay it back and they say, ‘You have these fees to pay,’ and you say, ‘I did not notice them,’ and they say, ‘Well, they are on the back in fine print.’ But at least some people would read it. There is an opportunity here for the beneficiaries, if you like—the fund managers—and I am sure they would be prepared to spend some money advertising or helping in that way. I have not seen a migration pack for years so I do not know whether you have inputs from commercial companies. It would be an idea to.

Senator BUCKLAND—If the current fund was performing particularly strongly, is there provision for you, if you wanted to, to transfer money to that fund?

Mr Gribben—I do not actually think that I am allowed to pay into it because it is an employer fund. They consider it closed. I am working for the same company because it is a worldwide company. I am pretty certain that I am not allowed to pay into it. I have made no attempt to pay into it. I would rather pay into the one here. I have salary sacrificed from time to time. We have two kids in child care, so we are not at the moment.

Senator BUCKLAND—There is a common thread in your submission and in some of the professional submissions. Let me say, Mr Chair, that this is one of the better individual submissions that I have seen to an inquiry.

Mr Gribben—Thank you very much.

Senator ALLISON—In relation to the tax arrangements in the UK, would you be taxed on pension funds?

Mr Gribben—Current law, as I understand it, is that you do not get taxed on growth. When you get to retirement, you have to buy an annuity, in effect, with the pension fund. If they are paying that pension to you, they normally deduct what they call in the UK basic rate tax. I am not sure what the current rate is, but it would be in the low 20s. I understand that under Australian law they allow you to claim part of that payment as a return of principle—of course, it is an annuity—so about eight per cent or something of the annual amount you pay you can claim as a tax deduction.

CHAIR—Is that a tax rebate?

Mr Gribben—It is something like that. In relation to the UK tax that they have withheld, which you cannot actually claim back, you can claim as having paid that tax in Australia, and they will give you a credit for it. In effect, depending on your tax rate here and on how much you are earning in retirement, you may pay no tax to the Australian authorities or you may pay just a little bit extra. That is my understanding of things. There is so much tax law and superannuation law that it is hard for an individual to get across it all.

CHAIR—In terms of the higher rate of reduction of the capital amount transferred, would you favour a law change to enable that amount of tax to be deducted through the fund rather than through the individual, because in most cases taxes are paid by the fund rather than by the individual, certainly at this early stage when you have not got an immediate entitlement to it?

Mr Gribben—I understand the point. I would still be paying the tax. It would still reduce my fund by 25 per cent. I am sure that, if I net present valued that to retirement, it is a negative for me. I am sure it would not be in my interest to do that. Because I am a high rate taxpayer—and let us hope I continue to be a high rate taxpayer—I cannot see that it is ever in my interest to pay nearly 50 per cent of the growth since 1993 in tax. To be fair, when looking at this, you have to be at least no worse off than you would have been if you had transferred it within the law at the time.

CHAIR—I know you have to take a lot of factors into consideration when you are considering transferring money from the UK but, if you have a reasonably high entitlement, naturally you would want to spread your risk. What would be wrong with part of that risk being in the form of a UK pension?

Mr Gribben—Having funds in UK is a natural hedge against the weak Australian dollar, providing the currencies do not start moving in line. If they both become weak, it is not much of a hedge, in the same way if they both became strong. Australian superannuation funds are allowed to invest internationally. To be quite honest, I am not entirely sure where my Australian funds are all invested. They have a little portion that is overseas, probably about 10 or 15 per cent, and the rest of it is in Australian shares and Australian fixed interest. So that is also a hedge. But of course I cannot work out the specifics from the Australian fund. I understand the point. But I think if you are intending to live in Australia then your expenses are in Australian dollars. To have a hedge like that is really taking a view that the Australian currency is going to continue to decline. It is not a view that I share—it is people who are much more expert than me.

CHAIR—Thanks for expressing your confidence in the Australian system. Perhaps this would be a good place to finish.

Senator HOGG—The markets have just risen out there now!

Mr Gribben—Australia is a very wealthy country. I think people in Australia at times do not quite appreciate it as much as people from overseas do.

Senator HOGG—I do not know if you are prepared to express a view on this: if the parliament sees fit to put legislation through that addresses the broad issue—without being

overly precise about it at this stage—do you have a view as to when that legislation should operate from?

Mr Gribben—Do you mean if we wipe away the 1994 legislation and replace it with something else?

Senator HOGG—I am just wondering should it operate prospectively or should there be an element of retrospectivity? There are problems caught up with that. That is what I am interested in.

Mr Gribben—That is right. In fairness to the people who have transferred money and paid tax at potentially high rates, I suppose retrospectivity could affect them detrimentally in that they complied with the law, paid 40 per cent tax or something, and now you might change it to 15 or 20 per cent tax. They perhaps could feel that they would like that money back.

Senator HOGG—I wanted the view of a private citizen at this stage. I will undoubtedly ask that question of the—

Mr Gribben—The tax consultants.

Senator HOGG—Yes, and the other people later on.

Mr Gribben—I suppose we do not mind retrospectivity. If we are brutally honest about it, if retrospectivity is in your interest then you are quite happy to say it should be retrospective. If it is not in your interest, you do not like it. Would that be a fair answer?

Senator HOGG—That would be a fair answer.

CHAIR—There being no further questions, we thank you, Mr Gribben.

[9.33 a.m.]

SKINNER, Mr Andrew Bryden, Vice-Chairman, Superannuation Committee, Taxation Institute of Australia

CHAIR—Welcome. Your statements are protected by parliamentary privilege and all that that implies. If you wish to make a request to the committee that certain aspects of your comments be in private we will consider your request. I would not expect that would be necessary because we are not expecting to ask you the amounts of moneys involved in a personal capacity or anything like that. We are interested in establishing the broad principle and the impact of this legislation.

Mr Skinner—I do not anticipate that there would be anything that we would need to say in private. We are looking at the legislation and how that operates. I thank the committee for the opportunity to come and appear this morning. I know that you are extremely busy and you have quite a few things on your agenda. I have noticed various reviews happening. Superannuation, as the senators would appreciate, has evolved substantially in the last 20 years or so and has become a very complex beast.

CHAIR—Would you like to speak to your submission?

Mr Skinner—Yes. In our submission dated 9 May there is a bit of background about the institute and the number of members we have. You will notice in the third paragraph we say that the encompassing issue of the committee's inquiry is the lump sum payment from a non-resident and non-complying fund, and the treatment of that.

Senator HOGG—Could you clarify about your 11,000 members: are they individual people or are there corporate body members?

Mr Skinner—To be a member you must be an individual. So they are all individual members. They are predominantly tax agents and people who work in the tax profession all around Australia. We have members from most aspects. It is very broad ranging. Often you will find there will be one or two people in an organisation who will join the institute, basically representing their firm. You may have a firm of 20 people with only one member of the institute, but effectively you are getting information to and from the 20 people.

Our basic submission is that the foreign superannuation amount should not be treated as income and there should be greater flexibility to encourage the transfer of money into an Australian superannuation system. I will go through some of the specific details, but that is our premise: we do not believe it should be treated as income. Superannuation benefits are an affair of capital, effectively corpus of a trust. The legislation is assessing them as income. We do not believe that is equitable.

My first specific point is about section 27CAA treatment of payments from eligible non-resident superannuation funds. I presume there is an understanding of that term. Effectively, it is a fund which is a superannuation fund but because it is non-resident it can never be a complying

fund under our rules. A lump payment is then assessable unless it qualifies as an exempt foreign termination payment. In order for that to happen, the payment must be made within six months of the taxpayer becoming an Australian resident or ceasing foreign employment. As you would appreciate, six months is a very impractical, inflexible and very short period of time. It can be extremely difficult for a person taking up residence in Australia to organise a transfer of their superannuation from the foreign fund within that time frame. In my experience, the average time taken to seek a transfer is in the order of two to three years, by the time the person has become a resident in Australia, is able to demonstrate to the foreign fund that the fund they wish to transfer into is eligible, and they satisfy all the various conditions. Even then, a lot of times those foreign funds will not entitle them to transfer all of their superannuation.

Senator HOGG—Are you referring specifically to any foreign country?

Mr Skinner—Most of the transfers I have done have been from the UK to Australia.

Senator HOGG—So you are speaking mostly about the UK?

Mr Skinner—Yes, and the UK have very specific rules on what they will allow in terms of the Australian fund. Their preservation rules and things like that are different. Nevertheless, even if you do manage to achieve a transfer yourself and get the whole lot out—I cannot remember the exact terms—you often have to keep a minimum amount in the UK system.

Senator HOGG—Does that two to three years apply to other foreign countries as well?

Mr Skinner—You can never transfer out from some jurisdictions. From memory, Singapore will not let you transfer out. You cannot transfer out from the United States unless you give up your citizenship. Most Americans, even if they are a resident of Australia, find giving up their citizenship abhorrent. They end up being locked into those funds; they can’t get their funds unless they satisfy some very stringent conditions.

It should be borne in mind that Australia is unique in the superannuation world. Most foreign funds, of course, are pension funds and do not pay much in the way of lump sum benefits. You can look at Singapore, the United States and Europe. New Zealand has virtually no superannuation system, anyway. So the first point is that we believe there should be a longer period than six months. It is often impracticable or impossible for people to apply in this amount of time.

The other problem is that some people become residents and then, for whatever reason, change their minds. They might not like it in Australia; the job does not work out and they go back to the UK. This means they become a non-resident again. You really do need something which aligns more with the visa requirements under which they are working, so that you have some concrete and objective view of what they are doing in Australia.

Another point is the need for clarification between the different provisions of the tax act. I have been working in the income tax area for 22 years or so. Owing to the sheer enormity of the legislation—and I have brought a small sample with me in case I needed to look at it—there are often inconsistencies between things. Some of those inconsistencies are, for example, between the foreign investment fund rules—the so-called FIF rules—and the operations of the ETP rules

which are contained in section 27. In some circumstances, an entitlement in a foreign superannuation fund will fall within the FIF rules and therefore you are taxable on an attribution basis, so the growth in the value of your investment is taxable. Then, when you receive your entitlements, there is potentially another double taxation aspect there, on that fund.

CHAIR—One or two witnesses have suggested this but nobody has actually said that there is double taxation. So while, in theory, it would appear it is possible, in practice we have not had any examples of people who have been subject to double taxation. Is it just a hypothetical situation or is it real?

Mr Skinner—I think it is real. I will find out some more details. I was talking to another tax professional yesterday about it. He raised the issue. I can make some inquiries.

CHAIR—You are not the only one who has raised it, but when we have pressed the issue, both within the committee and outside the committee, people say, 'It's possible but we don't think it could happen.' So I would like clarification of that. I am sorry for interrupting but it is a very important point.

Mr Skinner—I will see whether I can find some actual case examples where people have had double taxation applied to them under the FIF rules. From memory, there was an exemption in the FIF rules for employer sponsored foreign superannuation funds.

CHAIR—Yes, it is the personal funds that are most at risk.

Mr Skinner—The personal funds potentially have got that double taxation. The double taxation is a possibility and that is something we need to explore to see if the evidence is happening that way. Further, it is not clear that section 23AK, which is one of the exemption provisions, would provide appropriate exemption from the operation of section 27CAA in such cases involving FIFs.

CHAIR—That might be another one you might wish to explore.

Mr Skinner—That is the same sort of thing. The third point there is probably a more general thing. Back in 1980 or so there was no taxation on superannuation. The funds were exempt from tax and the benefits at the other end of the day if they were taken as the pension were taxable at the marginal rate without a rebate and lump sums at five per cent at marginal rates, which was a system that meant that nobody ever took a pension except public servants who had no choice. During the 1980s there have been many reforms. In 1988 the taxation of funds commenced and 15 per cent was levied on the income tax of the fund. At the time marginal rates were still around about 60 per cent and ETP tax rates had gone to 30 per cent at the time and they came back to 15.

Effectively what we are saying here is that the average tax rate on a superannuation member is around the 15 per cent mark or higher. For the vast number of superannuation members now, under the current system of the GST and lower tax rates, they are paying an average tax rate which is often greater in the fund than they are paying in their own right, particularly for people returning to the work force working part time. My wife, for example, works three days a week in a hospital—she has gone back to nursing—and her superannuation is actually taxed at a

higher marginal rate or higher effective rate than her own income. So there are quite a lot of inequities there and the taxation of super has basically stayed constant as marginal rates and average tax rates have come down. If this erosion continues, we will end up with the situation where a substantial number of members will be even further worse off. Then there is the surcharge. On top of that you have the reasonable benefit limit problems which are referred to here. To transfer money into an Australian superannuation fund from overseas then brings it into the Australian reasonable benefit limit regime. There is meant to be symmetry between the RBLs. In other words, the employer—

CHAIR—But there is a concession, though, isn't there?

Mr Skinner—Some of it is undeducted, basically, and that is the value on the date you became a resident. The increment in the value to the date you transfer may be a greater increment which then links up to the RBL. But you are bringing to an account some money that has not been concessionally taxed.

Basically the third point refers to foreign transfers or encouraging people to transfer into the Australian super system. If they leave their money in the UK, the United States or wherever it might be, their income accruing in that fund is tax-free until the time they retire, therefore leading to a greater potential benefit. If they transfer it to Australia where there is taxation on the fund, potentially surcharge and other things then their accumulation will be less. If people start making decisions based on income tax rather than economic rationality or for simplicity, they will end up with money in another fund.

Our fourth point applies to defined benefit funds. A lot of foreign superannuation funds are still operated as defined benefits schemes. The trend to accumulation basis or contribution basis is very strong in Australia but in America and the UK they still have a lot of defined benefits schemes which are where your benefit is expressed as a proportion of your years of service, some multiple of salary and some other factors. A typical defined benefits scheme is one where you worked for 20 or 30 years and it was only at, say, ages 50 to 55 that you had a rapid accumulation of invested benefits. You may have a very long service period but a very low accrual of benefits.

Then there is the date of transfer into an Australian fund from a non-resident fund. Let us say that they work for a company like Shell, they come here at 45 years of age with 15 years of service and stay in the Shell fund because they are still working for Shell in Australia. They continue to accrue their benefit multiple, but the majority of their benefit accrues in the last five to 10 years of working. Rather than saying that they have had 25 years in the fund—10 years in Australia and 15 years in the UK—as far as the fund is concerned, their benefit multiple is mostly accruing in the last couple of years when they are in Australia but realistically it is in the entire period when they have been in Australia and out of Australia. What happens with a lot of these situations is that the employer is concerned that their employees are no worse off working in Australia than working in the UK or anywhere else. The employer will either have to compensate the employee—for example, if they choose to come out of the Shell fund—or the Australian entity will be charged the cost of maintaining the superannuation benefit for the member. From my experience in dealing with corporates, I know that a lot of these sorts of problems cause a great deal of angst because executives and others coming to Australia are insistent that their superannuation is equivalent to what it would have been had they stayed

where they were. That discourages people from shifting here. So there is a punitive effect on taxation.

What are we saying at the top of the page 3 is that it would be fairer to tax only the proportion of the total super benefits which relate to the service of the member. In other words, what we are alluding to here is that there is a concept of eligible service period in the income tax legislation. If you are in a fund for 30 years, your service period is pre post 1983 proportionally and the calculation of your pre 1983 and post 1983 is simply on a day's basis. What we are alluding to is that a similar thing should happen: it should be a day's basis calculation based on their service period.

One of the other problems with the operation of the act—this is point 5—is that when a member transfers in they may be personally liable for an amount of the tax but not have access to any of the funds. So it is treated as though it is income of a member. The payment of the tax liability cannot be met until they retire. The precedent for allowing the member access to their funds to pay this tax liability is already in the act. For example, you can commute a pension to pay a surcharge liability which arises after you have left the fund or have started to take your benefits, and there are a few other precedents which allow for access to preserved money to pay liabilities. It would be consistent with the operation of the existing law to say that you can commute or you can take a lump sum to pay the tax liability. Alternatively, you can pass the liability back to the fund, which the funds do not like because it increases their administration costs, but they do not have that many transfers coming in. The main problem there is that the member is liable.

Point 6 is in regard to the interpretation of the relevant day. It is a technical term used in the operation of the provision and you will see in the second paragraph that it is the day on which the taxpayer became a member of the fund or the first day during the period in which the relevant payment relates to when the taxpayer became a resident of Australia. We believe it gives an interpretation problem of what the relevant day is. It is best illustrated by an example where a person has come in and gone out of Australia several times, which is not unknown. On 1 July 1980 a non-resident becomes a member of a foreign fund. In 1990, they transfer to Australia and become a resident and there is $500,000 in that fund. In 1995, they become a non-resident again and in 2000 they come back in as a resident and now there is $750,000 in that foreign fund. On 1 July 2002, they are still a resident and there is now $1 million in the foreign fund and they wish to transfer to Australia.

The problem with that scenario is this: what is the relevant day—1 July 1990 or 1 July 2000? The liability may be $1 million minus $500,000 or minus $750,000. So the taxpayer, in seeking to understand this, in self-assessment would probably err in favour of themselves and take the later relevant day, which is 1 July 2000, making the liability on transfer $250,000. Of course, the commissioner examining this would probably err on the other side and take the earlier date. We do not know.

Senator HOGG—I cannot believe that.

Mr Skinner—What, that the commissioner would take the other date?

Senator HOGG—Is this an actual case?

Mr Skinner—I have seen situations like that where people have come and gone several times in their working life.

Senator HOGG—Has it been tested by way of a tax ruling?

Mr Skinner—I am not aware if a tax ruling has been applied for or tested in that respect.

Senator HOGG—It is one thing for you to put to us a hypothetical case. It is another thing to put to us something that is a reality.

CHAIR—What has been in question, though, is the period. In terms of residence, is it tax residence, which is a far shorter period, or is it permanent residence, which obviously gives a little bit more leniency? Would you like to comment on that? What is your preference—tax residence or permanent residence?

Mr Skinner—If the act uses the word 'resident'—and it normally refers to resident in the context of being a tax resident—I would interpret it as being from the time that you became a tax resident, not a permanent resident. In essence, the scheme of the act uses the words 'a resident for tax purposes'. It is defined in section 6. Therefore, that is consistent unless it is using a different term in that provision. Without looking that up, just off the top of my head, I am pretty sure in both cases it uses the word 'residence' in the interpretative provision, section 6, and also in your section 27CAA, so I would take it as being a tax resident, not permanent resident.

CHAIR—Yes, that is what it is, but what should a fairer interpretation be—citizenship or permanent residence?

Mr Skinner—The thing with tax residence is that it tends to be somewhat retrospective. If you come to Australia and you end up spending 183 days here in a year you then become a tax resident from the date that you arrived and took up occupancy. It may not be the date that you are granted permanent residency. From a tax perspective, looking at the various rulings on that, the commissioner's view is that if you come here as a visiting lecturer and work at a university, although you are only on a three-year tenure, you are a resident for tax purposes from that first year that you take up your position in the university. I cannot recall the actual ruling number—it is in the 2,000s—but there is quite an extensive one where the commissioner puts forward his view on residency. It is a very encompassing ruling. It does not take much for a person to become an Australian tax resident. I believe that then brings in your foreign superannuation entitlements. You then leave again, and whether or not the revenue should have got something in respect of your superannuation entitlements becomes a jurisdiction problem because you are back in the UK, Canada or wherever else you came from, and of course it is much more difficult for the revenue to get it. That is what we are doing there. I have also put together a few additional comments, which I will leave with Peter, on some of the foreign superannuation issues which expand on a couple of these issues. I might leave them with the committee to consider.

CHAIR—If you would like to table the documents, they will be included as part of your submission.

Mr Skinner—They treat some examples that a colleague had given me a couple of days ago, talking about a lot of funds where vesting does not occur until very late in the period of fund membership. So on the date you become a resident, your accrued benefit is virtually nil. In the UK post office fund, for example, there is no entitlement until 55 years of age. If they come here before 55, their benefits are caught but their vested benefit is nil. At age 56, they then have a benefit of £100,000—with our exchange rate, that is $300,000—and of course they have a substantial tax liability. What tends to happen with this, I believe, is that people do not declare a lot of these payments, so there is probably a high degree of—how shall I put it? The hearsay evidence I have seen is that you inform people of these liabilities and they are not very happy, so they either arrange to go back to the UK when they retire, spend the next five years back in the UK and live off their superannuation, and then come back to Australia again; or else they simply believe that they do not have to declare it and that therefore they will not get caught. Of course, with the double tax agreement exchange of information, eventually these things do come through.

One other point, which is slightly beyond the scope of the taxation of transfers, is in respect of the splitting of superannuation in the event of divorce. I have had a number of dealings with irate members or their clients who are recipients of foreign superannuation pensions and have now been divorced. They are still assessable on the full amount of their pension in Australia, although the wife has, as far as, say, the German rules go, been allocated 50 per cent of the pension account—just like what we are moving to in Australia. So the problem with the taxation of foreign super is that we are also moving away from taxation of benefits under the member's name, allowing splitting on divorce; but that is only in respect of Australian superannuation funds. So you have non-residents receiving money from overseas and paying tax on it, and their ex-spouses are entitled to the benefits under the divorce provisions. So there are probably quite a lot of other inconsistencies there.

Senator ALLISON—Mr Skinner, could you explain for me how the Australian government calculates the growth on a pension scheme?

Mr Skinner—For a defining benefit pension scheme? Yes, I can.

Senator HOGG—We cannot record the pause in the *Hansard*, but it would be worth while recording it.

Mr Skinner—It is really the responsibility of the member to find out from the fund the value of that pension account on the relevant day that they become a resident. Predominantly, for example, they would receive a member's benefit statement, which would say, 'Andrew, you have been in the fund for 20 years and your accrued benefit is this amount'—or your vested benefit or whatever terminology they might use. So it is not so much the government coming in and saying, 'What are the rules?' or 'What has the fund told you is the value of your account?' Say—in one of those extreme cases—it is the guy of 50 years of age in the UK postal workers fund. The value, as far as our rules are concerned, is nil. Then what happens is that you have a nil balance when you become a resident in Australia, you receive your money at 60 years of age or whatever it might be, and that entire amount is therefore taxable in the Australian context. The defined benefit schemes and things are difficult because you really are reliant on the information you have provided and how they define your benefit entitlement.

Senator ALLISON—Or the growth. Aren't we talking about the growth period in which your—

Mr Skinner—The growth is just going to be the increase in the value of your account.

Senator ALLISON—Is that the increase in the value of your pension entitlement, or what?

Mr Skinner—I would probably have to go back and look at the legislation again just to refresh my memory, but, if you are speaking of someone who, at 60, only gets a pension from the UK fund of, say, £10,000 a year indexed for life, to ascertain the value of that you would have to apply some sort of commutation factor based on implicit earning rates. For example, in the Australian context we have actuarial tables, reproduced in the act, for valuing an income stream like that. It may be a multiple of 17 or 18 or 19, depending on various factors. That gives you a lump sum value of that. But, as to what the actual act says, I would have to refresh my memory, because most people I have dealt with recently have been accumulation members. You get a bit hazy after a while, trying to remember everything.

Senator ALLISON—But you said earlier that there were few accumulation countries.

Mr Skinner—Overseas, a lot of them are defined benefit schemes, but you may still take a lump sum at retirement from some of those.

Senator ALLISON—Which countries would be in that category? It is not Singapore or the US.

Mr Skinner—It is mainly the UK. A lot of the UK schemes are old defined benefit schemes. Some of the American schemes are defined benefit—some of the larger corporations.

Senator ALLISON—The committee has speculated as to the reason for these laws, and assumes it is to prevent Australian residents from putting their superannuation entitlements offshore and avoiding the taxes on the fund.

Mr Skinner—That is correct.

Senator ALLISON—In your experience, do many people attempt to do this?

Mr Skinner—When the amendments were made in 1994—and I remember being extensively involved in looking at them at the time—they were designed to prevent Australian residents from using offshore super funds. Strangely enough, it was after that time that, I think, the incidence of using foreign funds increased dramatically. I did not think that most of those arrangements were effective. I do not think the majority of them would stand the test as superannuation funds, if you looked at them, because a super fund has to be for the provision of benefits in the event of retirement—the sole purpose test. Most of the foreign schemes that were set up as various arrangements were done more for a tax benefit. They were not really done for the purposes of other things. So, in effect, until that period I had not seen many instances where people were using foreign funds to avoid tax on a mass basis.

Certainly, the rules were designed to tighten up and to seek to bring into the Australian jurisdiction as much of the superannuation money as possible. In particular, if a deduction for superannuation moneys was allowed in Australia, the intent was that those benefits effectively ended up back in Australia. I refer, for example, to the changes to the taxation arrangements for departing residents—the backpackers rule, so to speak, and the New Zealand shearers rule. When they leave now, the taxation on their fund benefits is at the highest marginal rate, or effectively a bit higher than that, so you look at the overall tax cost as being negligible. That is what we are seeking to do there.

What used to happen prior to 1994, however, was that you had more employers with a global superannuation arrangement. As I mentioned, let us refer to a company like Westpac or Shell in which people are transferring and moving around the world all the time. The employer is anxious to give everybody the same employment arrangements as much as possible, but every country has its own jurisdiction. The problem is that the corporates will tend to put their tax arrangements in the jurisdiction which gives them the best outcome, so you then get the problem of tax havens like the Netherlands Antilles, or whatever it might be this week, and they set up their global system there. There is certainly friction between the leakage of revenue and overseas superannuation arrangements.

Senator ALLISON—So should we be looking specifically at the corporate sector for this leakage? Is that the aim of the law?

Mr Skinner—I am thinking more in the past about that sort of tension there. Most of what we have spoken about today has been inward transfers—the taxation of inward transfers—into the Australian system. So you have somebody who is coming into Australia from a tax exempt system and they will be taxed at the rate of 15 per cent on the accrual, some undeducteds and then the benefits are subject to RBLs et cetera. They are coming into the fold, so to speak. What we want to try to do is encourage them to bring their money to Australia and hence lead to that increase.

With respect to the rules for money leaving Australia and going into foreign superannuation funds, the way they should work is that if it is a contribution to a non-complying fund, there should be no deduction, and fringe benefits tax applies. So you effectively get a double whammy—a 30 per cent penalty to the company and a 48.5 per cent FBT benefit. I am not aware of much leakage going out anymore, but it is something that one could explore in greater detail.

CHAIR—What was the nature of the development in terms of consultation when section 27CAA first came in? You said you had some involvement. Who was involved? The explanatory memorandum is very vague.

Mr Skinner—Yes. I remember—with the Taxation Institute—the draft bill appearing in 1994. I cannot remember if it was before or after the effective starting date; it was probably after the date. We looked at the provisions quite extensively and had some input. I could probably even find some of the submissions that were made at the time.

CHAIR—You might like to take it on notice.

Mr Skinner—Yes, I might. I could probably find some of them.

CHAIR—Take it on notice because we have time constraints.

Senator BUCKLAND—On a slightly different matter, we are talking about bringing funds to Australia, and I can understand and agree with the benefits that come with that. How receptive are the Australian funds to this type of thing? I say that on the basis that it is often quite difficult to roll over from one fund in Australia to another. I would like your views on that.

Mr Skinner—A lot of Australian funds do not want to entertain transfers from overseas, particularly if they have to give a condition to those funds where those transfers are coming from that the moneys will be preserved until preservation age, which might be 60, or something like that. Also, if there is potential tax liability to Australian funds, they will be concerned about the types of liabilities they are opening themselves up to. What tends to happen is that people often set up a self-managed fund arrangement to do the transfer into.

Senator BUCKLAND—A self-managed fund would be quite difficult. For someone like me, it would be almost talking a foreign language—as I am doing here today—with a tax consultant or anyone like that. I would not be competent to have a self-managed fund.

Mr Skinner—That is right.

Senator BUCKLAND—Does that not then create a real difficulty when we are talking about this issue of transferring funds?

Mr Skinner—It certainly does because you have a great problem with a typical master fund, a corporate fund or, particularly, an employer fund. If you come to Australia and start working for BHP, or someone like that, it is unlikely that they would want to entertain a transfer from an overseas fund, simply because they do not necessarily understand what they are getting and what liabilities might be imposed upon them for doing that, bearing in mind that trustees and administrators are concerned in it. A lot of times the money does stay over there because it is so difficult to get transfers through. There are a couple of consultants around who specialise in the transfer of foreign superannuation money. I am aware of a firm in Perth that does a lot of transfers, and their fees are not cheap—potentially something like five per cent of the amount transferred.

Senator BUCKLAND—I am wondering whether this inquiry will achieve very much if we have legislation that allows the transfer of funds but we have fund management schemes or funds that are not receptive or prepared to accept those funds. What are we achieving?

Mr Skinner—I suppose the question is to what degree can we succeed. If there is greater simplicity and certainty in respect of what the obligations of the receiving fund are, it should become easier for those funds to then accept these transfers. If there is uncertainty and their advisers say that this might happen or that might happen and that this is a problem or that is a problem, of course, the funds will say that it is too complicated. If there is certainty on those taxation arrangements, you may not necessarily get the fund resistance. It also becomes a matter of competition after a period of time. If there are a lot of people transferring money into

Australia then of course more funds are doing it, so there is greater demand and greater competition, and systems eventually come to grips with that.

Senator BUCKLAND—Are there requirements for new legislation or different legislation to accommodate this or to put demands upon the funds to start accepting overseas transfers? It worries me somewhat, I have to say.

CHAIR—Wouldn't it be true to say that, while corporate funds may have some hesitation, most public offer funds would readily take the money?

Mr Skinner—Most public offers would except if they have to give a preservation restriction of a different age than the Australian rules have. I looked at the HESTA's report summary yesterday. They have 400,000 members. If five of those members have a preservation rule of 60 or 65, and everybody else is under standard preservation rules, it is extremely difficult for the administrator to track that little bit of money which has to be preserved. The problem with administration is that the more complex it is, the greater the cost, and of course the greater the cost, the lower the return to members because the members will pay the admin. It is a difficult thing, and I have not come to a firm conclusion as to what is probably the best way for it to be.

Senator BUCKLAND—I have listened to your evidence as intently as I can and there is one issue I want to be very clear in my mind about. You talk quite extensively about the definitive interpretation of 'relevant day'. I am not sure that I have it in context and I have tried to listen to what you have had to say. What is the institute's attitude—that is, the body that you are representing—to using something like the day upon which you obtain citizenship as becoming the relevant day in the context as you have it in your document? Am I in the right context?

Mr Skinner—Yes, you are in the right context. Using the day that you become a citizen, or the date that you are granted permanent residence, is an objective test which makes it very easy for the taxpayer and for the adviser to be able to say, 'This is the right day because that's the bit of paper that shows the day you became a citizen,' or 'That's the day you were granted permanent residency.' That is an objective thing and you do not have the problem of trying to interpret what this particular provision means. With anything to do with the tax act and the tax laws, the greater the certainty the easier it is to comply with. The greatest way to get certainty is to have a third independent reference point, if you know what I mean. I agree with what you are saying—the date of citizenship would be the ideal date.

Senator HOGG—I think you will need to take my first question on notice. I note that you have 11,000 members.

Mr Skinner—Yes.

Senator HOGG—I would therefore expect that you would have some idea of the extent of the problem that we are being asked to address as a committee. Without giving the names and addresses of individual cases, do you have an analysis of the problem? Are 65 individuals affected and is the amount that is in contention $10 million or £100 million—something like that? Are you able to give us that sort of analysis? I am not asking you to go into a very deep analysis.

Mr Skinner—We use an electronic communication in the form of a newsletter that goes out to all the members every week. In that, we often request members to respond and tell us what their experience is in a particular area. We can certainly make that request of the members and see what sort of response we get. I suppose another time when we get exposure is when a member has a problem for a particular client and they come to the tax institute to see if something can be done. The other way to find out also is for me to speak to some of the people I know in the large accounting firms that deal a lot with migration. There are particular areas in some of the large firms that do a lot of migration work.

Senator HOGG—The reason I am asking for this is that we are being asked to address a problem; we were given a specific case in the first instance that drew our attention to the issue. But if we had not been given that case and someone had not pressed it with us, then this inquiry might never have taken place. If there is a difficulty out there, that has obviously been around since 1994, then there has not been a thunderous thumping on the door to say, 'Hey, we've got this big problem. It's stopping X millions, hundreds of millions of dollars, from coming in by way of superannuation. There is this problem of the taxing of the benefit and people's ability to bring the money into Australia.' If you could give us some idea about that, that would be helpful.

Mr Skinner—I will do that for you.

Senator HOGG—If this committee recommends to the parliament and the parliament sees fit to pass legislation, when should the legislation operate from? Do you have a view on that? If you do not, could you take that on notice as well and get back to us?

Mr Skinner—As a tax practitioner, anything retrospective—either good or bad—is abhorrent. I suppose if it is in the taxpayer's favour it is not quite as abhorrent but the point is that as an adviser you need a situation of certainty. So if the law says this today, I want to know tomorrow, when I wake up in the morning, that it has not changed with respect to what it said yesterday—nothing fills you with greater horror.

Just as an aside, I spend my life advising on superannuation and have done so for 15 years. I had a call at eight o'clock one Sunday morning from an old couple who got an excessive benefit determination because of an administration error. If you want to look at the situation of people dying because of RBL problems, I have had a couple of cases where I reckon that we almost had to have the oxygen there, because they get this bit of paper out of the blue and it says, 'This is your tax bill,' and someone looks at it and dies. But the point with retrospectivity is that, even if it is a good change, I think you have to have very good arguments to make that change retrospective to the date. My suggestion would be to give people plenty of notice, set a date into the future and say, 'This is the way it is going to be.'

Senator HOGG—Your having said that raises the next question. If you set a date into the future—and I have an open mind on this—will that slow up the process for some transfers that might be in place—

Mr Skinner—They are so slow anyway that I don't think it will make a lot of difference.

Senator HOGG—That is all right. It is just that I think we need to be aware of this.

Mr Skinner—If the date were, say, 1 January 2003 then that is not that far in the future—or even 1 July 2002. Having things start in the beginning of a tax year is nice from our perspective. I think we just have to live with the way the system has been since 1994; I do not think it could be contemplated for it to be retrospective to then. But maybe there should be some transitional rule for those cases. Let us take those people who have no accrued benefit until they are 55. If you then brought in a rule which says it is based on service period—however many years you are a non-resident and how many years you are an Australian resident—there is an element of retrospectivity in the way that calculation will then be used to assess their liability.

Senator HOGG—That was one of the criticisms of the existing legislation: that even though it operated from 1994—

Mr Skinner—It is in its effect retrospective.

Senator HOGG——it was retrospective itself. That is why I am asking the question.

Mr Skinner—That element of retrospectivity should be removed, and we should try to come up with a situation which is not retrospective.

CHAIR—Thank you very much.

Proceedings suspended from 10.26 a.m. to 10.42 a.m.

ANDERSON, Dr Michaela, Director, Policy and Research, Association of Superannuation Funds of Australia

HODGE, Mr Robert, Senior Policy Adviser (Tax), Association of Superannuation Funds of Australia

CHAIR—I welcome the representatives from ASFA. You understand the rules under which we operate so we invite you to speak to your submission.

Dr Anderson—Thank you for the opportunity to speak here today. In our submission we have drawn attention to the fact that a number of our members over quite a long period have expressed concern about the transfer of benefits to Australia. The three issues that are central to ASFA's concern are ones that you would be familiar with because you probably heard them earlier with Andrew's submission. The first one is the difficulty many people face in meeting the strict six-month time limit for completing the transfer. Within the submissions—I have read most of them—you have examples of some of the problems. I notice UniSuper, particularly, setting out some of the problems with the overseas fund feeling satisfied that it can transfer to Australia. I am mindful that there have been some changes in the UK, and Robert might later speak about some of those. I should also say that when we were trying to understand whether the UK had made it easier to release funds for transfer we became just as bogged down with the rules as we do with the Australian system, which was both saddening and heartening that we were not the only people who do not manage these things particularly well.

Senator HOGG—I thought there was a bit of tongue-in-cheek there.

Dr Anderson—Just looking at that six-month time limit, where an individual is deemed to be tax resident on a number of different occasions over widely separated years while continuously being a member of the same fund, the relevant date for vesting is the date on which they were first tax resident in Australia. That is our understanding of it. One of the things that has been drawn to our attention about that is that fixing the value of the overseas benefit at that date is sometimes quite difficult. In fact, the overseas funds have on occasions refused to do it. The example that was given to me very recently was that an American fund, the Unilever fund, point-blank refused to do it for an Australian fund: they will not fix the value at a date. They will tell you the figure, but they will not go back and fix the value at the date that we require it on.

Senator HOGG—Why is that? Too hard?

Dr Anderson—Not their business, too hard and just go away, seems to be the message that I was given. That is one example, in that you do not always have good cooperation from the fund on the other side because we are wasting their time. The member is going and that is the end of it. The other issue there is that there is no definition of 'properly payable' in the sense that you have to look at the benefit that was properly payable to the member at that relevant date. The example that Andrew Skinner gave here this morning was of the post office fund where the person did not have the full vesting until they were aged 55. I think that is quite interesting because, in one sense, although he was arguing that the accrued benefit at the date of the

transfer was in fact nothing and it did not vest until age 55, I think you could probably mount a case that there was a benefit properly payable to the person when they turned 55 and it should have been applicable there. The only point I am making here is that what is properly payable is not without difficulty. I will give one more example of that, in the Australian context. If you have a fund overseas that is like one of our New South Wales public sector funds, when you leave, your benefit is just the leaving service benefit, which is much lower than the deferred benefit you can get when you are 55. So, in that example, which is the one that is properly payable: the resignation benefit, which is much less, or the one that you could get when you turned 55? We have examples of these sorts of things in our own jurisdiction, and I think we should be looking at 'properly payable' very closely.

The second point that we see as an issue is the inability of individuals to access the transferred funds to meet the tax liability following the changes to the preservation rules. This seems to be one that causes great concern, because people often do not realise that they are going to have this tax bill and just do not have the funds to meet it. If we do nothing else, I think we have to make them able to pay the tax—although I think we should do more than that. All of this probably becomes more of a problem because of the general lack of knowledge of individuals about the rules and the repercussions of not meeting those rules. I think that is an issue where people get into situations and do not know that they are in them and that they are going to have difficulties until some time down the track. That is not the kind of situation that we want our citizens or our permanent residents to be in.

We have proposed two changes to the existing arrangements and one is to extend the six-month period to two years. We think this would be sufficient time for most transfers to be undertaken and would make allowance for the fact that for many the decision to permanently locate in Australia is taken beyond the current six-month limit, so we are suggesting two years. We think that would probably fix most of the issues. Where an amount is taxed under the provisions of section 27CAA—that is, the two-year limit is not met—we think we should apply the flat tax rate of 15 per cent to the amount to be included in assessable income under the provisions. The 15 per cent tax rate would approximate the rate applicable had the growth in the value of the account occurred within an Australian complying fund. Robert will add to that later.

As a final word, we would caution against making this even more complex. If anything, our solutions must be simple. Some of the submissions put forward solutions that look very good until you analyse them in terms of simplicity. That is the caution we would make there. We want funds to be able to deal with them but, more importantly, we want members transferring overseas benefits to be able to understand them. We do not want to get into situations where we have lists of approved funds from overseas. That would be a nightmare to deal with. We are very wary of pre and post dates. If they are to be on the agenda, we should look very closely at them. Also, if possible, we see value in trying to set tax rates, if we are going to change them, to rates that are already there with appropriate rationale for putting them in at those levels. That is all we wanted to say. We welcome questions.

Senator HOGG—You would have heard me ask previous witnesses about the operation of changes. Do you have a view as to the operation of any changes that this committee might recommend and the parliament might look at?

Dr Anderson—One of the criticisms of the 1994 changes—to be honest, I cannot remember the 1994 changes—that I see is that this was not widely publicised. So it is not just the funds that we are looking at; it is probably the general public as well. We need to be aware of that. I do not know whether Robert has a view.

Senator HOGG—You may need to take that on notice and get back to us with a considered response—we would welcome that—and also the issue which has cropped up during this hearing of the retrospectivity of the operation pre-1994, which some people have claimed to be an unfair aspect of that particular piece of legislation in working out the amount to be taxable and so on. The only other question I have is the same question I have asked other witnesses today: do you have any hard evidence in a summary form of the extent of the problem? Do you know of 10, 20, 30 or 40 cases of this in the last eight years?

Dr Anderson—We have no hard figures on that but, just from looking at something like the UniSuper submission, I think there are probably particular industries, if you like, where this might be more prevalent and where people might be more likely to be moving.

Senator HOGG—Is this problem more likely to be confined to the more well-paid sectors in the community? Or is it something that can be characterised by a specific trade or profession? We had the case of visiting lecturers, for example, and people in education; I understand that it could affect doctors and nurses and people in the medical profession. Could it affect a range of classes of workers, rather than the broad spectrum.

Dr Anderson—Yes. When we are talking about all other places accept Chile not having compulsory superannuation, I imagine that there may be an element of certain professions having this. But, if you look at somewhere like the UK, the provision of employer sponsored funds is quite prevalent, so I imagine it would be an issue that affects more groups than just those people who are in the professions.

Senator HOGG—If through your network and your organisation you could find some data for us, it would be helpful.

Dr Anderson—On that 1994 issue, one of the things that occurs to me—and it is something I spoke about earlier—is that the ability to find a figure at the relevant data is an issue. That may be a big issue if you are trying to look at 1994.

Mr Hodge—When you look at most funds, if a member permanently departs the fund or preserves their benefit and leaves the employment, the fund knows a benefit on that date. If that date is pre-1994, the fund, I believe, will have great difficulty in then determining purely for the purposes of Australian legislation what the benefit was worth on the relevant date in 1994. That then comes back to the Unilever issue, where you would find funds overseas refusing to do it because there is no requirement on them. It is something which is required by Australian law but they cannot be forced to provide it. That is why we would caution against going down the path of trying to determine what the accumulated benefit was before and after any given date. It is far simpler to work on a date that is known to the fund at a point in time, and that is the point when the member or the individual leaves employment and the membership in the fund is frozen.

Senator HOGG—If the parliament puts in place a regime of legislation that takes on the appearance of being fairer than the current regime, is there any estimate of the amount of super funds that might flow into Australia?

Dr Anderson—We have no idea of the funds that would flow in.

Senator HOGG—In your view would it be a considerable amount or are we trying to grapple with a problem that is very small at the margins?

Dr Anderson—This is just a gut reaction: I think you would probably find that most people who wanted to bring funds in would be bringing in reasonable amounts; I think that they would be people who were trying to rationalise or get their life together, if you like, in a new country and they would have considerable funds. That is just a personal reaction.

Senator HOGG—There would be an economic benefit too, I assume if we could free up the regime and make it attractive for those funds to come in? That is repeated in a number of submissions.

Dr Anderson—Definitely. The amount that would have been transferred in on an individual basis would probably be quite considerable.

CHAIR—Would ASFA be in favour of having a shorter period, where the situation would be that you gave the commissioner power to exercise a discretion—for example, where it has taken an unusually long time for the fund in the UK to provide the information?

Dr Anderson—I am somewhat wary of everything being left to a discretion.

CHAIR—Not everything.

Dr Anderson—But you are talking about a very short period and limited discretion.

CHAIR—A shorter period, yes. I am not saying necessarily six months, but a shorter period. You have suggested two years. Say we came down to even one year, but with a discretion, how would you view that?

Dr Anderson—It would be an improvement. I am not sure how well the commissioner would respond to more discretion.

CHAIR—Looking at your fine print, your proposal is to permit, but not to actually require, a fund to release enough of the transfer to meet the tax. How would that work in practice?

Dr Anderson—I think we are cautious about that at the moment because we have not actually been able to go to our full membership to see whether requiring funds to release would pose any real issues.

CHAIR—Could you come back to us, because it is fairly cardinal.

Dr Anderson—We will come back to you.

CHAIR—How would ASFA regard a proposal for either the ATO or APRA—or both together—to establish a transfer protocol? The absence of a protocol seems to us to be at the core of one of the problems, in terms of delays.

Dr Anderson—Would the protocol be between the other jurisdiction and—

CHAIR—An established protocol in terms of the transfers, to make sure the language, the forms et cetera are identical.

Dr Anderson—It would be excellent, except that—

CHAIR—Is it practical for that to happen?

Dr Anderson—I do not know that it is practical. In some ways, I suppose, since a lot of the issues that have been raised with us have been UK based, there may be some real value in even establishing some protocol with the UK. It seems to me that it is more difficult to establish protocols of this nature with, say, the US, so once you go beyond that I am not sure how well we would go. But certainly there would be some value in dialogue between Australia and the UK at least, since they have actually changed some of their rules; that might be useful.

Senator ALLISON—Can I ask about the example you gave of Unilever not being prepared to fix the value? What then happens in practical terms? Is some estimate made of it?

Dr Anderson—I am not really sure of the outcome of that. It seems that, at the moment, there is a dialogue going on between the Australian fund and the overseas fund to try to get past this impasse.

Senator ALLISON—And the dialogue is between the tax office and the fund?

Dr Anderson—No. It is between the funds, I think. My understanding is that it is between the funds—to see if the Australian fund can talk them around into providing more information.

Senator ALLISON—What happened with the tax office? Did the fund go to the tax office and say, ‘We’re having difficulty with Unilever; they will not tell us. What do we do?’ Did the tax office say, ‘Go back’? How was the tax office handling this?

Dr Anderson—I do not have enough information to answer that, but I can get you a better outline of the whole case, if you would like that.

Senator ALLISON—Can you give the committee some idea of an average or typical growth amount and comment on the impact on older people versus younger people? Is there an unfair burden on those who have accumulated more—in relative terms, not in absolute dollar terms?

Mr Hodge—I think that would be extremely difficult to obtain because of the way in which the law is applied. It is driven by tax residency. Section 27CAA very clearly states that you

determine the value on the date on which you first become a tax resident. Once you have been in Australia continuously for 183 days and meet with the rules set out in the ATO determination, you are then deemed to have been a tax resident from the date on which you arrived. So at that stage your six-month period has gone, if you have not already transferred your money. Where people come to Australia for a period of six months or 12 months—say, a teacher might transfer from the UK and work in a school for 12 months—go back to the UK for four or five years and come back again and then decide to settle, then the date on which they first became a tax resident is the date when they first came to Australia. So you have this gap. How it impacts upon an individual depends on whether they have attempted to do the transfer when they first came to Australia or at a later period when they decided to stay in Australia. That is why there is probably some merit in one of the proposals which seemed to look at the idea of taking it from the date you last became a tax resident but with some caveat put in to stop some anti-avoidance measures. It is another reason why we believe the period should be something like two years. Because tax residency dates back to the date you first arrived, then the six months has gone immediately. Then you have to go through the rigmarole of determining the overseas authority and what information they need to allow the transfer to be made to Australia. It is generally after people have been Australia for more than six months that they decided to reside here permanently. It is a different situation for people who visit Australia and then decide to stay and people who emigrate to Australia.

Dr Anderson—The question is the amount. With that as the background, it is very difficult for us to know what the amounts are, because they are not actually related to the fund and our information comes through the funds. These are individuals.

Senator ALLISON—I understand.

Dr Anderson—I cannot answer that one and I cannot answer the one in terms of age, either, because it is not fund information; it is individual information.

Senator ALLISON—But, intuitively, you would imagine this provides a greater disbenefit to older workers than those who have less accumulated. Would that be fair?

Mr Hodge—Insofar as older people tend to have a higher balance, the growth component on top of the balance is greater. Intuitively you would suspect that older people are more impacted. Older people in Australia would also generally tend to be on a higher wage rate and therefore on a higher marginal tax rate.

Senator ALLISON—Dr Anderson, I think you said you had read the submissions. Can you comment on the Australian Taxation Studies Program submission which suggests that the transferred amounts should be taxed as capital gains? Have you had a chance to consider that recommendation?

Dr Anderson—I will hand that to my colleague.

Mr Hodge—They look at it being taxed as capital gains insofar as, if you had put a lump sum investment in an overseas fund and then you withdrew it 18 months later, the growth could very well be regarded as being a capital gain. As pointed out in another submission, part of the

growth within a fund is from income and part is from capital growth, so by taxing it as a capital gain you would lower the effective tax rate.

I think that is where they are coming from; they are saying that a capital gains tax would be more appropriate. We would like to look at it from a different point of view and ask ourselves: had the money been transferred into the Australian fund within the relevant time and had it then grown in the Australian fund, how would that money have been taxed in Australia? It would have been taxed as income to the fund and whether it was a realised capital gain or income growth, it would have been taxed at 15 per cent, generally, in the fund, being derived from an investment, in an overseas unit trust, say.

Senator ALLISON—What about administratively; would it be tidier from the fund's point of view if the capital gains dealt with the growth at that point in time and you picked up the situation from then on?

Mr Hodge—What we do not want to do is complicate the process.

Senator ALLISON—That is my question: does this complicate it or make it easier for you?

Dr Anderson—We feel it makes it more complicated. That is the reason for our 15 per cent.

Senator BUCKLAND—I want to stay, for a moment, with the question of six months versus two years. Where did the two years come from? Who dreamed this up? Was there a meeting? It is consistent through the submissions.

Dr Anderson—It comes from experience of how long it takes to get the overseas fund to get itself into a state where it can transfer.

Senator BUCKLAND—That is really not the answer because if that were the case—and all the submissions were saying the same thing—I would think it would be 18 months, two years or three years, but consistently it is two years. I am just wondering whether an association had a meeting and they voted. What is the story?

Dr Anderson—There are some here that are saying one year.

CHAIR—One says 10 years.

Dr Anderson—I think that is looking too pessimistically at the UK system—but not too much. When you look through some of the submissions that provide examples of their experiences, they are probably coming around to 18 months or two years. I think that is where the two years came from. Those that are saying one year are saying—as you said, Senator—there should be some discretion of the commissioner if things really bog down in the transfer.

Senator BUCKLAND—Is the cause of the delay in dealing with the issue at Australia's end or in the country where the funds exist?

Dr Anderson—It is a mixture, I think, in terms of the person realising that they have a problem: that they need to transfer. I think one of the submissions puts it very well: when you are changing countries, fixing up your superannuation is not the first thing on your mind, so by the time you focus on it some time has elapsed. Then, by the time you go back to your country of origin, understand the rules there and then put them into practice, considerable time has elapsed.

Senator BUCKLAND—You said earlier that what is properly payable is 'not without difficulty'. I think you used words along those lines. Could you expand upon that a little?

Dr Anderson—I do not have the legislation in front of me, but the rules say that it is 'the benefit that was properly payable at the time of the relevant date'—or something like that. The words used are 'properly payable'. The problem is that defining what is properly payable at that time is a fairly contentious issue and it probably needs to be better defined because, as I said, what was properly payable at a particular date—and the post office example, I think, is an excellent one—was nothing. In fact, it was only nothing because you could not get it until you were 55, so it is almost nonsense to say that there was nothing payable in that instance. If we are going to do anything, we need something there; 'properly payable' is not enough to guide funds or anybody.

Senator BUCKLAND—Would that vary between countries of origin? We have heard a lot about the UK. Would it vary between that country and some of the European countries—say, Germany or France?

Dr Anderson—It would depend on the fund rules, presumably, and potentially government regulations about payment might come into play as well. So it is not an easy one. I think, in the history of that 'properly payable', we are probably looking at an attempt to stop people using the section inappropriately. We can agree that that is not what we want, but using the term 'properly payable' probably did not get us a good outcome.

[11.17 a.m.]

MACKENZIE, Mr Gordon Donald, Senior Lecturer, ATAX, Faculty of Law, University of New South Wales

CHAIR—Welcome, Mr Mackenzie. You are given protection of parliamentary privilege for attending, and, if you wish some parts of your presentation to be made in private, the committee will consider your request. But we do not expect that you will make such a request in this particular inquiry. Thank you very much for appearing before the committee today. We invite you to speak to your submission.

Mr Mackenzie—By way of introduction, I would like to thank the committee for allowing ATAX to present its submission. Before I go into detail, I would like to give the committee a bit of background about what ATAX is and what it does. It is a dedicated school for tax practitioners in the Faculty of Law at the University of New South Wales. It is staffed by economists, lawyers and accountants. My own experience is that I have been with ATAX for three months. My training is as a lawyer. Previously, I was group taxation manager at AMP. I have had experience in superannuation in Australia, New Zealand, the US and the UK.

I will now speak to ATAX's submission. ATAX believes that it is a timely period to look at these rules, which were introduced in 1994. They have been in place now for eight years, and it is timely to review whether they have been efficient and fair in their performance. The committee has no doubt had explained in detail the operation of these rules, but broadly their effect is to tax amounts accumulated in foreign superannuation funds for individuals who have taken up Australian tax residence and who have not had those amounts paid to them within six months of taking up that residence.

ATAX's view is that the experience of the application of the rules is that they are producing inefficiencies and inequities. In terms of inefficiencies, in speaking to practitioners and, indeed, in my personal experience, most foreign superannuation funds will only release accumulated amounts to an Australian superannuation fund if the Australian fund agrees to preserve those amounts until some time in the future—usually when the member retires from employment. That can have a result where the rules at the moment actually give the tax liability to the individual; the individual has a liability but the funds are in a superannuation fund, creating a mismatch of funding.

There are other problems that ATAX sees with these issues, in that quite often—certainly with UK superannuation funds—they can take a long time to release the funds to an Australian fund. Alternatively, they can require those amounts in the UK to be preserved and not released until a significant amount of time after the individual has taken up Australian residence. That causes a bunching effect, in that when the accumulation after taking up Australian residence is transferred to Australia it can be a significant amount of money and it can push the individual's tax rate to the highest tax rate, whereas, if they had derived the income over the period, it would not have had that effect.

Again, ATAX is of the view that the current rules overtax the payments. In our submission we have drawn a parallel with a foreign mutual fund which has had income accumulated in it. If an Australian resident was to exit that fund, then those amounts would be taxed as a capital gain in

Australia, excluding certain anti-avoidance rules. Also, in terms of overtaxing, I think the starting point is that the funds that we are talking about have been committed to a retirement savings purpose in the foreign jurisdiction. If you compare this system of taxing them at the highest marginal rate with the way that we tax retirement savings in Australia, clearly there is significant potential for overtaxing. Given all those circumstances, ATAX's view is that the amounts accumulated after taking up tax residence should be taxed as capital gains in Australia.

I welcome the comments by ASFA about our submission, and would just point out that perhaps taxing these amounts at the rate they would have been taxed in the Australian fund, had they accumulated here at 15 per cent, is again probably an overtaxing. Whereas 15 per cent is the nominal rate of most funds, because of the effect of imputation credits and so on, the nominal rate—as the committee would well know—is usually reduced to six or seven per cent. In addition, part of these accumulations coming from overseas could indeed be distributions of surplus by the fund, which would not be taxable had they been distributed in an Australian fund. So presenting a fiction of taxing these amounts as if they had been accumulated in an Australian fund creates distortions. ATAX's view is that the only fair way of dealing with this is to tax these amounts as capital gains.

Finally, one of the inefficiencies in the existing rules—which I have already commented on—is that the liability goes to the individual, even though funding goes elsewhere. ATAX's view is that if these amounts were taxed as capital gains then whoever was the recipient would in fact suffer the tax liability as well, and we could avoid the problems of mismatching funding.

CHAIR—What do you mean by the recipient? The fund or the individual?

Mr Mackenzie—We are suggesting in our submission that if amounts go to individuals then they would be taxed as a capital gain to the individual.

CHAIR—How could they go to an individual if they were preserved?

Mr Mackenzie—That is quite correct. You would imagine that the number of times that it could go to an individual would be minimal, so there is virtually no risk to the revenue in providing for that.

Senator ALLISON—But the fund pays the capital gains tax?

Mr Mackenzie—Perhaps I have not made myself clear. What we are proposing is that these amounts, regardless of who receives them, are taxed as a capital gain by the person that receives them.

Senator ALLISON—So the fund would pay the capital gains tax?

Mr Mackenzie—If the fund received it, it would pay the capital gains tax; if an individual received it, he or she would pay the capital gains tax. As the chair pointed out, the chances of an individual receiving these amounts is very minimal.

CHAIR—If we follow your proposal through and make the amount subject to capital gains tax, is not there greater opportunity for avoidance? If so, what would be the avoidance

opportunities by treating it as a capital gain? Are there any opportunities for tax avoidance that really made the requirement for section 27CAA to be necessary or written into the act at all?

Mr Mackenzie—Our view would be that what we are proposing creates no greater opportunity for avoidance than any of the other proposals. One could envisage that if somebody was intent on using these rules inappropriately then they would set up their own small superannuation fund in Australia, set up a foreign fund, accumulate amounts in a foreign fund and then transfer it into an Australian fund to participate in that. Avoidance is always an issue. Being an experienced practitioner in the tax field, you have to ask yourself whether indeed the rules always have to be put at the lowest common denominator to protect against avoidance. In our submission we have pointed out that the general anti-avoidance provisions, part IVA, have successfully been used against foreign type exemption schemes, and we would not see that being any different for individuals.

Senator HOGG—I think you are probably the correct person to put me straight on the operation of the foreign investment funds legislation in respect of the current provisions that we are looking at.

Mr Mackenzie—Indeed I am. I have been on the pointy end of some interesting tax office audit activity in foreign investment fund rules, so I have a very close working knowledge of them. In terms of these provisions, my understanding is that foreign superannuation funds are excluded from these provisions. We would be proposing that that would not change, that there is a specific exemption from the foreign investment fund rules for foreign superannuation fund accumulations.

Senator WATSON—But not personal superannuation funds, which are increasing in popularity in the UK—that is the problem. Employer type schemes, yes, and the government schemes, but the problem will be increasingly important because of the encouragement that is given to personal super, which appears to fall outside the scope of this exemption.

Mr Mackenzie—I understand. Certainly when I was in the corporate world, on behalf of some industry bodies I negotiated those foreign investment fund provisions and certainly the exemption of superannuation funds from those. In that process I identified that if superannuation funds per se were exempted from foreign investment fund rules then there could be a significant avoidance issue there.

Senator HOGG—Can you just clarify for me: when did the foreign investment fund legislation operate from, given that we are looking at the specific case operating before 1994 and the effects there. Did that foreign investment fund legislation operate prior to 1994?

Mr Mackenzie—To give you the precise answer to that question, I would need to take it on notice. My recollection is that it was in about 1991 or 1992 that those rules were inserted into the act.

Senator HOGG—As I understand it, from some of the submission I have read, it operated in conjunction with 27CAA; is that correct? There was a possibility of a double tax there; is that correct?

Mr Mackenzie—Yes, that is correct.

Senator HOGG—Are there any proven cases of that happening?

Mr Mackenzie—Not in my experience, but it is worthwhile pointing out that the foreign investment fund rules are unique in a certain way because they in fact do not tax individuals on receipt of money, they tax individuals on an accumulation, whereas 27D actually operates on a receipt or payments basis.

Senator HOGG—Do the foreign investment fund rules apply retrospectively as 27CAA does?

Mr Mackenzie—I think what you are asking me is: do the foreign investment fund rules have application to accumulations made before the date of their introduction? Again, to be perfectly correct, I would need to take that on notice. My recollection is that they probably do not. There is a step up of accumulated values at the date of introduction of the rules. I would be happy to have a look at that in more detail.

Senator HOGG—If you could take that on notice and answer it, that would be interesting. I have asked other witnesses today two questions: the first relates to evidence of the extent of the problem. Do you have any evidence either in terms of the number of cases where people have been adversely affected by 27CAA or any other arrangements?

CHAIR—Could you clarify your question.

Senator HOGG—The number of cases.

CHAIR—Adversely affected in what way?

Senator HOGG—Affected by not being able to bring the money in or paying the highest rate of taxation.

Mr Mackenzie—Prior to appearing before the committee, I spoke with some colleagues of mine who are members of the actuarial profession and who have practised on international corporate transfers. They say that it is a problem. I was unable to gauge the number of individuals it applies to except to say that it is certainly not a significant issue.

Senator HOGG—Do we know the quantum of money involved—is it significant?

Mr Mackenzie—Again, I would be happy to take that on notice and make inquiries of my colleagues.

Senator HOGG—The other issue that I have raised is that if parliament were to legislate to remedy what people perceive as being a difficulty under the existing regime, when should it legislate from? Should it be prospective or should there be an amount of retrospectivity in there? People generally do not like retrospectivity but some people may well argue that there is a case for some retrospectivity in this instance. I do not know.

Mr Mackenzie—As you pointed out before, arguably there is an element of retrospectivity in the rules as they apply at the moment because you can have amounts accumulated before 1994 that are taxed in 2002. In terms of the date of application, if the rules were to change today, then certainly any individuals repatriating funds from today, even though they were accumulated after 1994, would not be affected by the old rules. I would have thought that on balance there is an argument that the rules could be changed retrospectively to 1994 given the experience that inefficiencies have emerged.

Senator HOGG—If the rules were changed retrospectively to 1994, that raises the question: what does one do with all the transfers that have taken place thus far? How would one treat those?

Mr Mackenzie—That is right, and there are a couple of issues there. Certainly, I do not think the revenue would be at risk if you opened it up back to 1994, because those transactions have completed. So there is no opportunity to change that. There would be administrative issues in making sure that those people who returned their income to include these amounts had adjustments made to it. That would be difficult with the current rules which only allow amendments to be made in the prior four-year period.

Senator ALLISON—I will just come back to how the capital gains tax proposal would work. How does it compare in terms of a tax impost to the 15 per cent? You pointed out that 15 per cent is on the high side, given that nominal tax rates are more like six or seven. What would the effect of capital gains be as a percentage?

Mr Mackenzie—The way the rules work at the moment, superannuation funds are entitled to a one-third discount for tax on capital gains, so that indeed would make the nominal rate 10 per cent.

Senator ALLISON—Given the difficulty that many submissions have pointed to in getting the information about what growth is, do you see this alternative proposal as helping that situation or would it make no difference?

Mr Mackenzie—It would make no difference.

Senator ALLISON—And the capital gains tax would be applied at the point of entry into the fund?

Mr Mackenzie—Yes. We do not see any reason to change the rules for when the liability arises, so it would be under general principles of, broadly, receipt or entitlement—in your terms, when it hits the fund.

Senator ALLISON—And it would be applied to the moneys for that fund holder, not to the broader group?

Mr Mackenzie—Yes. My understanding is that superannuation funds do have adequate account keeping records to reduce that member's account for that liability.

Senator ALLISON—Treasury was unable to indicate to the committee what the likely revenue flow from this provision is currently, nor what the implications of changing it to something else might be. Presumably, you do academic work in your program. Have you hazarded a guess as to what this revenue might be currently attracting?

Mr Mackenzie—We have had a look at trying to get some measures of that, but it is very difficult and all we have been able to do is get anecdotal evidence. The indications are that it is not a significant amount of revenue.

Senator ALLISON—What is your measure of a significant amount of revenue? I know this is hypothetical, but I think the committee has no grasp of what we are talking about here.

Mr Mackenzie—Again, I am happy to take that on notice and to see if I can get some empirical evidence from discussions with my colleagues in the actuarial profession. There probably would be 50 or 60 people and certainly their clients are senior executives in large corporates, so they would be at the upper end of the scale. Hopefully, that will be of some assistance to you in working out the amount of revenue involved. Other than that, we do not have any indications of what it is likely to be.

Senator ALLISON—The committee secretary has just reminded me of some of the problems that Treasury and others face with the lack of useful data and the lack of disclosure of that data. Would you go so far as to say that there should be an improvement in the way that information is collected?

Mr Mackenzie—Certainly I would agree with that. The impression one gets when one reads the rules now, having had some experience with the changes in 1994, is that these are anti-avoidance rules. That probably explains why they do overtax. But absent any idea about the problem, they probably are in overkill.

CHAIR—Mr Mackenzie, when you were in the tax office, were the tax office worried that a lot of these moneys were coming to Australia but not being subject to tax at all?

Mr Mackenzie—Senator, I probably spoke a bit quickly. In fact I was not in the tax office: I was with AMP, as such. Andrew Skinner has just commented that it is the same thing. Indeed, with the number of audits that I went through with the tax office, I did feel as though I was part of Tax.

CHAIR—Did you get the impression from those audits that they were worried about moneys not being properly accounted in Australia?

Mr Mackenzie—Not for individuals; but certainly, for our corporate investors exporting capital, that was a significant issue for them. I joked before that I was at the pointy end of an audit issue on the foreign investment fund rules, and in fact the tax office were concerned about the application of foreign investment fund rules to Australian institutional investors. But my understanding is that they are not as concerned for individuals.

CHAIR—Thank you. As there are no further questions, we thank you very much for attending. It is always good to have people here from academia.

[11.42 a.m.]

BARRETT, Ms Jane Margaret, Superannuation Policy Adviser, CPA Australia

KELLEHER, Ms Noelle Eileen, Member, Superannuation Centre of Excellence, CPA Australia

CHAIR—Welcome. As a member of CPA Australia, I suppose I should express an interest.

Senator HOGG—You are declaring an interest, Chair.

CHAIR—Does either of you have any comment on the capacity in which you appear before the committee?

Ms Kelleher—Yes. I am a partner in Superannuation at Ernst and Young.

CHAIR—Thank you. I now invite you to speak to your submission.

Ms Barrett—CPA Australia and its Superannuation Centre of Excellence are pleased to appear before the Senate committee in support of our submission to the inquiry relating to taxation transfers from overseas funds. We recognise that the current legislation tends to prevent the abuse of taxation concessions applicable to superannuation, and tax avoidance more generally. We consider, however, that the legislation provides little incentive to members who have balances in overseas superannuation funds to have them transferred to Australia. This includes migrants to Australia, and those Australian who have been employed overseas for a period of time and have returned to Australia.

The tax rate, which is inconsistent with the treatment of accumulation of superannuation benefits in Australia, the capacity of the individual to pay the tax liability from their own resources, and the rigid six-month period result in a general reluctance to consolidate retirement assets into Australian superannuation funds. The result of this is an effective reduction on the amount of tax paid in Australia from benefits accruing overseas. There are also less funds available for investment in Australia, because overseas funds will predominantly invest in their own country and, we suggest, a problem with noncompliance with these tax provisions. In our submission, we outline various options for legislative reform for the committee's consideration. At this point we stress that we have not addressed in detail the administrative burden on funds, nor how any alleviation of tax may be funded.

We recommend that the committee consider the following amendments to the relevant legislation to remove any unintended consequences of the application of section 27CAA and to ensure consistency of tax treatment of income receipts by resident superannuation funds. These amendments include: that a period of two years, rather than six months, be allowed from commencement of residency to arrange for transfer of benefits to Australia without tax being applied to the transfer; that the amount transferred from the overseas fund that is assessable be taxed under the capital gains tax provisions at 10 per cent or as a contribution at 15 per cent; and that, where the transfer of funds is made to a resident superannuation fund, the liability for

the tax be passed on to the superannuation fund and the potential for double taxation be removed so that the exemption under the foreign investment fund provisions be extended from employer sponsored funds to personal foreign superannuation plans. We are happy to take questions from the committee. Thank you.

CHAIR—Ms Kelleher, do you wish to make any supporting comments?

Ms Kelleher—Not necessarily. I will answer any questions that are asked and we can go from there.

Senator BUCKLAND—I do not have many questions, because I am starting to get overloaded on this now. There are a couple of things that occur to you as you go through proceedings, and unfortunately you are going to get the questions. Can you help me with one aspect of transferring funds from overseas? If a person determines they are going and are able to transfer their funds from an overseas fund to an Australian fund, is there ability for them to partially transfer their funds and take the other part as a cash payment, perhaps to set up their house or to do whatever they want with that part of the money?

Ms Kelleher—It would probably vary from fund to fund and you would need to look at the rules in the overseas country as to whether or not those superannuation fund moneys could be taken out as cash, as a lump sum or as a combination; it might even get down to the specific fund rules. When you are looking at transferring benefits from overseas funds to Australia, you need to look at what we do in Australia and say, ‘Okay, how do the overseas jurisdictions deal with that?’ If the member went to an Australian superannuation fund and said, ‘Look, I want to take out my benefits, and I want to take some in cash and roll over some to another fund,’ the fund would have to look at whether or not they could pay out some of those benefits as a lump sum. If they were subject to preservation, regardless of what the member says, they could not do it. If the overseas fund were in a similar situation, they would not be able to take out any portion as a lump sum.

I think in the UK there are circumstances such that you could take, say, 25 per cent of your benefit as a lump sum and 75 per cent as a form of pension. If you passed all the criteria in terms of getting access to that lump sum benefit, you could be in a situation of taking some of it as a lump sum and some of it as a transfer into an Australian fund. Presumably you would be in the same boat as you would be in here in Australia, so if they were preserved benefits you would have to meet age requirements and other things along those lines. In terms of whether the overseas benefits give access to buying a house and those sorts of things in Australia, it is probably better to start with a prima facie ‘no’ and then that would be subject to whatever rules there are in the overseas jurisdiction.

Senator BUCKLAND—So that would vary from fund to fund, and I understand fund rules and how that would work. Would there be a difference between a company or an industry fund and a private fund?

Ms Kelleher—It could be very different, I would think. Again, you have to overlay the country’s rules on the type of fund that you are looking at. Trying to say, ‘Okay, all funds of a particular type have the same set of rules,’ could be extremely difficult and the same as saying, ‘Well, here in Australia if you are a corporate fund you have this set of rules and if you are an

industry fund you have another set of rules.' Dealing with benefits that are effectively preserved like ours is the same when going from fund to fund, but you are looking at the preservation rules that are applied overseas.

Senator BUCKLAND—In respect of the funds overseas that people would be wanting to bring to Australia with them, once they passed that defined date, to your knowledge—and this may be a question that is not easily answered—do they have anything like our preserved amount?

Ms Kelleher—A lot of countries do have a form of preservation which can vary from fund to fund and from country to country. What we have seen in terms of people trying to transfer benefits out into Australia is that they have been trying to transfer them before they have reached that particular age category that they have to reach to get access to the benefit ordinarily. The overseas fund is trying to make sure when they transfer the benefit into Australia whether it will be subject to a comparable or a similar preservation regime or benefit payment type to that expected in the home country. If you have got a benefit coming from a UK pension fund, they might be saying a person can go into an Australian pension fund that is actually going to pay out a pension for the life of the individual. They might be doing that when the person is 40 or 45 or it might be happening when they are 60 or 65, so it varies.

Senator BUCKLAND—I asked a question of a witness earlier this morning—I do not know whether you were here at the time—and through the question and the answer it was established in my mind that some funds in Australia are quite reluctant to take overseas transfers. I can understand that—they are reluctant to take rollovers from our own country. What is the position or the attitude of CPA Australia to that? Do you have a position on that? I suppose it is a policy issue. What is the attitude of CPA Australia to the transfer of funds into Australian funds and the reluctance of Australian funds to accept overseas money?

Ms Kelleher—I will comment on the funds side and I will leave you to comment on—

Ms Barrett—The superannuation funds having a reluctance to accept that has not really been raised as an issue, but I guess I can take that on notice and talk to a range of members who are involved with superannuation funds. I certainly was not aware of a reluctance to accept a transfer from an overseas superannuation fund.

Ms Kelleher—Our experience is that funds would like to be able to accept the transfers coming in, but a lot of them find the tax issues off-putting or difficult to deal with inasmuch as I suppose we have not a lot of clarity in terms of where they should be taxed. Should they be taxed under 27CAA, which is taxing the individual, or should they be taxed under 274(10), which is taxing the super fund? So they have had difficulties in determining what should be done from that side. Then they have also had difficulties with equity issues. If we are receiving those benefits and the individual has to pay the tax, how do we justify that? Do we want to deal with issues of members saying to us, 'We want some money because we have got to pay tax and we have not got any other money except for what is in the superannuation?' They have found it difficult on that front to actually say comfortably, yes, they are prepared to accept these dollars coming in from overseas funds.

The funds that I have dealt with that have raised this as an issue have generally proceeded with the transfer but on the basis that they have done health warnings to the member concerned to ask them whether they are aware. So they are trying to act in the best interests of the members. But the whole tax issue has certainly created issues from a fund's perspective.

Senator BUCKLAND—In respect of shopping around for the most appropriate fund, what is the process? If you have a client come to you saying, 'I have got this little pot of gold back in the UK,' what is the process? Are they able to nominate themselves or do they look at the industry fund they are in? I would just like to be clear on that process.

Ms Kelleher—What we would be saying to someone who is coming to us—

Senator BUCKLAND—I am not asking you to commit yourself where you cannot.

Ms Kelleher—No, that is fine. We would be saying that you can approach the fund that you are in to see whether it accepts it. But a lot of the decision as to where that money is finally transferred is actually going to be driven from the overseas fund's perspective, because the overseas super fund is actually going to want to satisfy itself that, if it is releasing money before it should, it is going into the kind of super fund that meets its requirements. So it may be that the person does have to shop around to find a fund that is going to preserve the benefits until the appropriate age that is going to pay out a pension benefit as opposed to a lump sum or allocated pension. So they really have to establish what the overseas fund requires in terms of an Australian fund and then find an Australian fund that actually fits that profile in order to be able to do it. So it is a really time consuming process with toing-and-froing in terms of whether it can go into their existing fund or whether they have to find some other fund for the money to go into.

Senator ALLISON—I would like to come to the case study that you provided us with of Mr H, aged 61. For his fund to increase from $80,000 in 1992 to $231,000 in 2002 seems to me to be extraordinary growth. That would seem to me to be at least 10 per cent growth per annum. Is that typical of UK funds?

Ms Barrett—This is based on examples of an overseas defined benefit fund which increases with the age of the person. When they receive their benefit, they may be over 55 and so that entire amount would relate to their entire period of service. That would result in that big jump.

Senator ALLISON—Could you explain that a bit more? As I understood it, the pension related to the years of service and the salary level.

Ms Barrett—Yes.

Senator ALLISON—Surely the salary level would stay the same, as would the years of service.

Ms Barrett—That is right, but there are certain changes. Once someone is over 55, the full extent kicks in. The properly payable amount of the accumulated entitlement at the day you became a resident for taxation purposes may be a certain amount, and that may be your exit rate. But beyond the age of 55 you are entitled to your full amount and you have complete

access to that, so it will be a much higher amount. So there will be a growth in that period that is attributable to your whole service, not just your service since becoming a resident for taxation purposes.

Senator ALLISON—The tax office would nonetheless regard that as growth in the normal sense of investment in income.

Ms Barrett—That is quite correct.

Senator ALLISON—When this kind of anomaly has been pointed out to the tax office, in your experience, what has been their response?

Ms Kelleher—My experience with talking to the tax office on issues associated with these transfers is that they probably do not want to know, because of the difficulty with the wording of the legislation and the associated issues. When you look at section 27CAA, it talks about benefits that are 'properly payable' to a person, and there is no actual definition of what 'properly payable' is. It also talks about the benefits being properly payable to the taxpayer. In a case of, say, a benefit transfer due to preservation rules, there is actually no benefit that is properly payable to the member, because it has to go from one fund to another fund. So we have a benefit that is actually properly payable in respect of the member, but not 'to' the member.

So, from the tax office's perspective, I think they are also trying to make the best of a bad lot of words to try to get something that is workable. Certainly, the way the words work, if we ignore the 'to' it talks about 'benefits properly payable'. It is then a case of working out what those benefits that are properly payable are. Without any guidelines it is: 'Well, which end of the spectrum do you want to be?' It also ignores gains resulting from exchange gains and things along those lines.

Depending on the timing as to when you bring it in, you might have situations like this example where it is someone who is working with the same employer and it is the multiples that are kicking over creating the increase. You might have situations where it is the exchange rate movements that are actually generating big increases in the benefits. It is not actually changing the figures per se, but the exchange rates are causing more Australian dollars to come in. There could be a variety of reasons as to why there could get big movements.

I suppose the other thing is that when you are looking at 27CAA, it is a retrospective tax. Even though that came in during 1994, it actually could go back to when someone became a resident in 1974. That can cause a lot of concern for people that up until that point of time felt no strain or exposure in theory but thought, all of a sudden, 'I have this new provision that I have to think about that I never had to think about at any point of time.'

Senator ALLISON—You say the tax office does not want to know. Surely someone has to arrive at a decision. Is there a tax determination for individuals that just ignores the arguments? How are these matters resolved?

Ms Kelleher—There are guidelines issued by the tax office which basically say, 'This is what our practice is.' We have often said to our clients that we think that the issue should be clarified so that there are some firm rules in terms of specific circumstances. But from the

individual's perspective, unless they are bringing in huge dollars, the cost involved with going through the process of getting a private ruling for their particular circumstances far outweighs any benefit that they may get out of it. Then it is also a case of: should the super fund be doing it or should the individual be doing it? We have generally found that people just look at it and say, 'Okay. The cost is too prohibitive in order to try and get some sort of certainty as to what should be happening.'

Senator ALLISON—Sorry, I am still missing a step. Presumably accountants prepare a proposal for the tax office that says this is putting the best light on their client's case. In the case of Mr H, you would argue, 'Some of that was not due to growth at all but to changes in the maturing of the pension benefit. Therefore, we say it should be this much and not that much.' What does the tax office then do?

Ms Kelleher—I am not aware of anyone that has argued what is properly payable because of the cost of going through that process.

Senator ALLISON—So they just pay what?

Ms Kelleher—What they would do is look at the tax office guidelines. Going through this example, they would say, 'Okay. Originally we had $80,000. We have now gone to $231,000. That is the figure that we are putting in to the return.' One of the concerns I have is that a lot of people do not know about these provisions. Therefore, I suspect there is a lot of noncompliance out there not because of wilful noncompliance but because of ignorance. A lot of the questions that we get come from the super funds themselves that are being asked to accept these moneys or have members approaching them to say, 'Can I do it?' It is like, can they and what do we do? Then with our expat client program, if we have clients where the employer has the individual as part of our program with Ernst and Young, we will get questions coming from the individual. If you think about the number of people who do not use some of the bigger firms and the number of people who are heavily involved with super, it is one of those things that people just do not know about. I think there is a lot of noncompliance because of ignorance.

Senator ALLISON—If a fund comes back to the accountant and says, 'Can we accept this or not?' are they required to advise the tax department when such a payment is made? Is that process there?

Ms Kelleher—There is no reporting mechanism on the funds to say that, when you receive these transfers, you have to report them to the fund. Most funds would not treat them as taxable contributions. They would treat them as effectively undeducteds coming in. There would be nothing in the system that says, 'Overseas transfers come into this fund as a flag for the tax office, so let us go and see what has happened on the other side of the fence.'

Senator ALLISON—Should there be, in your view?

Ms Kelleher—You have two options. First, you could put the reporting requirements on the fund, which is another layer of reporting on the fund's perspective, which does make things difficult for the funds because they have then got to make sure that they have another account that they are identifying and potentially a lot of forms. Second, you could put the onus on the individual to do so via their tax returns or something of a similar nature. Personally, I would

hate to see the super funds get caught up in a tug of war or being the watchdog for something like this if we are saying that it is the individual's responsibility for effectively self-assessing transfers that they receive from overseas. If we are saying that the super funds should be paying the tax on it, we will probably end up with a different set of rules. It is like: who is actually responsible for paying the tax?

Senator ALLISON—It has been suggested by one of our submissions that there ought to be a register for all taxpayers intending to come to Australia to reside—a register of their membership of overseas pension funds. Do you think that would be useful by way of process?

Ms Barrett—That may not capture Australians who have been overseas for a period of time, who have come back and who are seeking to transfer their funds back to an Australian resident fund. That register could be quite onerous, really.

Ms Kelleher—When people are coming into Australia, super is one of the last things on their minds. When they are coming into Australia, it is like: 'I've got to get my job organised and settled; I've got to get the family settled.' And that is when the six-month rule becomes a bit of a problem, because it is at least six months before they even start thinking about super. A register would be useful, but it is a case of how you make it so that it is not an onerous exercise. If you say to people that instead of the six-month rule it is the two-year rule—so we bring it into line with some of the other super rules that we have, to do with residency of super funds et cetera—it may be that the leakage we potentially have of people not amalgamating their super et cetera would go away, because people have that two-year window to get their money into Australia and they have more time to focus on their super and get it in an orderly fashion. That would also make it easier from the Australian fund perspective, because they have that time up their sleeves to get things in place. The overseas fund would be prepared to transfer benefits into Australia because they have enough documentation to say, 'Yes, I give a tick on all my criteria that I need to sign off on before I transfer across.'

Senator ALLISON—Some submissions have talked about the need for the immigration pack to draw attention to this, but perhaps it is another box on the immigration form. It is a fair assumption to make that adults will have paid superannuation in their prior country of residence. There would be few exceptions, I imagine.

Ms Kelleher—Yes. Given the potential tax impost that can be put on these benefits, anything that we can do to bring it to people's attention sooner rather than later I think is a definite plus. There have certainly been issues raised as to whether or not the *TaxPack* accurately reflects what happens with these benefits or what people should be doing with their benefits. Again, though, that is happening at least six months after they have come into Australia when they are doing their first tax return. Anything that we can do earlier is certainly better than leaving it way towards the end. There are a lot of issues coming in with the immigration stuff. We have linked super and overseas super with a couple of different things. SG stuff and release of benefits is tied in with the types of visas that you have.

These rules are tied in with your tax residency as opposed to your visa status. It would be nice to make it a nice fit, so that whatever your visa status is that effectively flows into the taxation of your benefits, just so that we have consistency across the board. A lot of people do get trapped because we have one set of definitions or rules on one side of super, and we think we

know what that is, and then they go on and look at something different and find, 'Woops, it's a different set of definitions that I'm dealing with, a different set of rules.' Even changing these provisions to link in with the visa rules would be much better than leaving it as it is.

Senator ALLISON—Regarding the amount payable, you mentioned the difficulties in arriving at what that actually means. Is it your view that the legislation should spell that out more thoroughly? Is it possible? Are there so many variations that you could not anticipate them? How difficult a task is that?

Ms Kelleher—We would certainly like the words to be changed from 'properly payable' to 'properly payable in respect of' because that gets over the zero base. There are a lot of variations, so properly defining it in the legislation will be really difficult. To at least have some guidelines that say, 'Here are some example scenarios' and have the industry come forward with examples and saying, 'This is the view that we would take' or 'This is the view the tax office would take,' would certainly go a long way forward in terms of what is 'properly payable'. You have to deal with defined benefits, variable vesting scales, how to deal with exchange rate issues and a whole variety of things that you can come across.

It would also be nice to tie things in to how the foreign investment fund rules apply to this situation. When looking at the foreign investment fund rules, people use the term 'employer sponsored funds'. From an Australian perspective, we know what those are, but the FIF rules refer to funds that are maintained by employers and associates of employers. So what exactly is meant by that? Does it mean employer sponsored funds or does it we mean something else? Then there is the tying up of issues in terms of personal superannuation funds—how do we treat those as part of the package? How do the other FIF exemptions tie into this superannuation exemption which sits in the foreign investment fund rules?

I know a lot of people have brought to your attention that employer sponsored funds are outside the FIF rules, but there are also exemptions in there to do with foreign investment funds of less than $50,000, which fall outside the FIF rules, which may give some people a bit of breathing space. It does not give them any space in terms of going over $50,000, which puts them back into the framework, but it might give them a bit of space. There is also a five per cent threshold test, which ties the whole lot into how it fits with superannuation and the treatment of the benefits coming in, et cetera.

CHAIR—In recommendation (2), you talk about arranging a transfer of benefits, in terms of reservicing. What definition of 'residency' are you referring to? Is it tax or actual?

Ms Kelleher—The residency of the superannuation fund there is looking at the tax residency of the fund.

CHAIR—In practice, have you experienced cases of double taxation?

Ms Kelleher—I do not get involved with the individual side of things, but talking to the people who deal with our expats, yes, it is an issue for people who have been assessed under the foreign investment fund rules for their superannuation benefits and then finally decide, 'Okay, I'm going to bring those into Australia.' There is nothing to give them a credit for the tax they have already paid on one side of the fence to offset the tax that is being paid.

CHAIR—In practice, doesn't the tax office give you a credit for tax paid under either FIF or 27CAA?

Ms Kelleher—Not that I am aware of. I can double-check and get back to you on that.

Senator HOGG—Following on from that, just momentarily, part of the difficulty that the committee has is whether there is hard evidence of what is happening in this area. It is not a criticism of you, and I think you probably heard me raise it with the previous witness, as I have all day. It is not that I am in a rut and cannot get out of it. Are you able to assist us with that?

Ms Kelleher—I will see what I can find out for you. A lot of the difficulty is that when you start to explain to people that this is how it works they go, 'This is all too hard and I'm not going to deal with it until the latest possible point.' They might decide, 'Okay, forget about staying here in Australia; I'm going to go home.'

Senator HOGG—Even evidence to that effect would assist the committee. It is one thing for us to report on an issue but it has got to be one that is quantifiable in some way. Currently we have no hard evidence, from what I can see.

Ms Kelleher—I think you are going to struggle to get hard evidence. What you have got to look at is whether the rules that we have make sense and how can we change them so that they actually do make sense and do not become a hindrance and do not stop things taking place that in the ordinary course of events we would expect to see. I do not mean to be telling you what you should be doing, but that is certainly something that I would like to see come out of this.

Senator HOGG—I am only too pleased to listen. I am serious.

Ms Kelleher—That is certainly what I would like to see come out of this, that we end up with a system that is going to work, as opposed to something like, 'We know it doesn't work but we are going to leave it because we can't find the hard evidence that this is going to happen.' Part of this is that these rules have only been in since 1994 and we are sitting here in 2002, so they really have not been around for that long. As people start to approach retirement, that is when we will really start to see this stuff kicking in. Part of the reason why we do not have a lot of the figures is that a lot of people probably do not know that they need to be doing this. Therefore, you cannot even tell from your FIF income how much of this is attributable to superannuation per se. One of the positive things that could come out with this is a system that actually works.

Ms Barrett—CPA Australia is looking to do a superannuation survey in the next month, and I will endeavour to include an item on this particular issue and then get back to the committee on the results of that survey.

CHAIR—Thank you very much.

Senator HOGG—The question I asked before was this: if there is to be a change to the date of operation of that legislation brought in by the parliament, do you have a view? If you do not have a view now, could you take it on notice and come back to us? Some people are saying that there could be retrospectivity. Parliaments do not like retrospectivity.

Ms Barrett—Because of the difficulties associated with it, and Noelle might be able to add to this, we possibly should be looking at prospective amendments.

Ms Kelleher—If you did retrospective amendments, depending on how the amendments turned out, as to who was paying tax and on what and all the rest of it, you have got individual tax returns to amend and you have got superannuation fund accounts et cetera, to amend, and trying to unravel everything that has happened in the past could be extremely difficult. There is no mechanism that I am aware of so that I could say, 'Okay, if the tax office issued a notice to all these people with red hair, then everybody who was affected by these changes would actually know that they need to take the following steps.' It would be an ad hoc revision process in terms of capturing everyone who has been affected by this since 1994. You would really be relying on the quality of their advisers to be aware of the change that is retrospective so that they then go back and find their clients who have been affected by it and do the appropriate changes, whether it be at superannuation fund level or at individual member level.

Senator HOGG—Yes, I was not advocating retrospectivity, by the way. It is something that has been advocated.

Ms Kelleher—Yes.

Senator HOGG—Unless one answers those questions, those who feel aggrieved by the process will not understand why you cannot have retrospectivity in these sorts of matters.

Ms Kelleher—Perhaps you can look at something that gives the commissioner some discretion, so that if someone approaches them to say, 'Can we amend this?' the commissioner can look at the circumstances and say, 'Okay, yes. I am prepared to make a retrospective adjustment on how all this has been treated in the past provided the following steps take place.' You have to get it right for both the individual and the super fund.

Senator HOGG—That just triggered in my mind that you said there are probably a lot of people who are unaware of these provisions. If the legislation is to change, how do we, as legislators, overcome the ignorance on the part of those people who have ignored the provisions to date and the liability that would occur prior to the date of any legislation coming into force?

Ms Kelleher—The same as you do with any other change that goes through parliament. It is getting down to the advisers, et cetera, being aware of what is happening and then applying that to the client's particular situation. Superannuation is a unique thing, inasmuch as most advisers are going to look at tax reform and, in theory, have an idea as to what is going on there. With super, they might say that with super change you do not need to worry about it. But I am certain that, from the CPA's perspective, they would go through an information program with their members. I am sure the Institute of Chartered Accountants would do a similar sort of thing, and ASFA would do a similar sort of thing. If all the industry bodies get on board with it, which I am sure they will, then through those networks those changes would be picked up.

CHAIR—It has also been suggested to us that we should make the tax implications available on the migrant information forms, including the visas.

Ms Kelleher—Yes, those sorts of things would help.

CHAIR—Thank you.

Senator HOGG—Just following on, any change that is done in respect of 27CAA should be done in consultation with the CPA and other organisations?

Ms Kelleher—Yes, that is correct.

CHAIR—Thank you very much.

Proceedings suspended from 12.23 p.m. to 1.24 p.m.

FORSDICK, Mr Michael James, Partner, PricewaterhouseCoopers

CHAIR—Welcome. Do you have any comment on the capacity in which you appear before the committee?

Mr Forsdick—Yes. Generally, in my capacity as a partner, I advise clients who are affected by this particular provision of the tax act relating to the transfer of superannuation benefits from overseas.

CHAIR—Thank you. As we have all read your submission, perhaps you would care to speak to it.

Mr Forsdick—In our submission, we introduce the general point that retirement benefits are a very important factor in relation to individuals' personal wealth. People who come from overseas to Australia, particularly to live out the rest of their lives here, have become more and more focused over time on ensuring that their retirement benefits are being adequately dealt with. Often it is very desirable for somebody who is going to live the rest of their life in this country to have their retirement benefits here in Australia. That is not always possible; it depends upon the rules of the overseas country where they may have accumulated those benefits. But often, in managing risk and just having a say in controlling those retirement benefits, there is the desire that they be here within these shores.

Section 27CAA presents some particular problems for achieving that goal. Also, to put it in context, this country has a lot of people who come from overseas—imported talent. Personally, I came out here 20 years ago for two years. I suppose that is the way it is: you like the place and you end up staying here, and that is great. Hopefully, I brought some talent with me. We should encourage the right sort of people to come here. In fact, many multinationals in this global marketplace are looking again and again at what the barriers are to moving people around the world effectively—and the issue of retirement benefits often comes up as a barrier that we are asked to advise on. More specifically, the main issue with 27CAA is that it can result in an imposition of a tax at marginal rates on an element of the transfer of the benefit. The individual has to pay this out of their own pocket when, in fact, at that time they do not get their hands on any of the transfer money.

In a moment I will come to some particular technical difficulties with this provision but, first of all, I will espouse what I believe are correct principles when looking at this. In principle, I believe that any growth in retirement benefits when somebody is working in, and a tax resident of, Australia should be caught within the Australian tax net through the way this country taxes superannuation. Any benefits accumulated before they had any connection with this country as a nonresident should not be taxed by Australia, subject to any double tax agreements that may exist. Double tax agreements with many countries around the world tend to deal with pension arrangements; and that, for example, gives the right for Australia to tax pensions from overseas funds, even though they may not relate to Australian service. But the principle is that Australia should be able to tax retirement benefits to the extent that they relate to Australian service.

The tax applied on such benefits should also be consistent with the way retirement benefits are taxed in Australia: they are, within certain limits, concessionally taxed and so forth. Our system of taxing in Australia is not to impose any tax on the individual until the benefits are actually taken, but section 27CAA is not consistent with that. The taxing of super benefits in Australia, as I am sure the committee is aware, is very much on contributions. The tax on that is paid by the fund, the tax on earnings is paid by the fund, and it is only the tax on benefits that is paid by the individual.

A further principle is that the tax be easy to administer. Referring back to our paper, we believe that there is a need for 27CAA to be replaced by a different system, whereby any tax relating to the build-up of retirement benefits here in Australia should be met by the fund rather than by the individual. In our paper we gave four options. The first one is to continue with the current system but with the tax liability perhaps being deducted from the amount transferred from overseas. We do not favour that option, because it would present serious difficulties, particularly with UK transfers. The UK would not allow that to happen but would like to see the transfer coming across intact. So we do not favour that one.

The second option is to continue with the current approach but to limit the tax to 15 per cent, which is the standard rate of tax on investment earnings in superannuation funds, and that should be paid by the fund that receives the transfer. The third option is to not have any tax up front at all, but to leave the taxing of the amount until the benefits are received.

CHAIR—I cannot see any difference between option No. 2 and option No. 1 in that you have to first convince the UK authorities before you can go down either route 1 or route 2. Whether you are taxing it at the marginal rate or at the 15 per cent rate, if the UK authorities will not allow it, we run into the same problem.

Mr Forsdick—We do. The UK's primary concern has been that the money is transferred intact into the Australian fund, which would not happen under option 1. Under option 1 a reduced amount would actually be paid into the Australian fund. Under option 2 that is achieved but then the Australian fund would pay tax to the ATO and, sure, that would reduce the benefits. I accept your point. I suppose it may be one step further removed from it not being transferred intact, which is what I believe the UK authorities would be concerned about. But it is a good point to make. Under option 3, as I said, we could leave any taxing until right at the end when the benefit is paid out, and that element that would otherwise have been taxed comes out as something called an untaxed element. An untaxed element is actually taxed at a rate that is 15 per cent higher than normal superannuation benefits. That is more consistent with the general operations of taxing on superannuation of overseas countries in that they tend to tax benefits at the end anyway. Coming back to the senator's previous point, the UK is not going to be too concerned with that sort of system because that is consistent with the benefits of tax being paid at the end when the benefits are taken, rather than the UK benefits being taxed earlier on.

The fourth option is to treat it more as a contribution and to tax it at a special rate. We do not favour that one because of the complexity that that may involve. On balance, we favour option 3. One of my principles was that it be easy to administer—which is very close to the hearts of many people in the superannuation industry—and to introduce an untaxed element could be seen as an extra burden of administration. The only thing is that there is not an awful lot of this going on, but I accept that that could be a negative.

Senator HOGG—Wouldn't your argument for ease of administration therefore favour No. 2 rather than No. 3? The money comes into the fund, it is taxed at 15 per cent and then—

Mr Forsdick—It loses its character.

Senator HOGG—the fund has no worry about tracing that element right through the history of the continuation of that fund.

Mr Forsdick—That is true. It is a balance between the concerns about it being taxed up front that maybe the UK have and the administration. Our conclusion was that it was really option 2 or option 3, but we would probably prefer No. 3. Our option is still No. 3. because we would prefer to leave it until the end.

Senator HOGG—We had a submission earlier today pleading with us not to go to a pre and a post situation, and it just seems to me that that is a pre and a post situation.

Mr Forsdick—There are some real technical difficulties with 27CAA anyway. At the moment, it is a provision that is a catch-all fix on benefit transfers but there are some real technical problems with it. Firstly, I think it is fair to say that not many people are aware of it. One of the technical difficulties is that 27CAA is actually triggered if I move benefits from one fund in the UK to another fund in the UK. Here I am, I have been working in Australia for a couple of years and I decide that my UK pension benefits should transfer from one fund to another and I do a rollover, if you like. That would technically trigger 27CAA.

CHAIR—Or if the company decided to change its fund?

Mr Forsdick—Or the company decided to change its fund. I may be working for a multinational and I am out here working for the subsidiary but I continue my membership of the fund in London and then make some alternative arrangements. I do a transfer and that technically triggers 27CAA which could result in me having a tax bill with no equivalent income or anything like that.

Senator HOGG—You could quite conceivably not be aware of that. Is that correct?

Mr Forsdick—Correct. In fact, to take that point further, let us say I decide not to transfer my benefits here but I am going to take the pension out of the UK. I have been in a UK pension fund for many years, and now I am going to take a pension. That is pretty straightforward. It means I will be taxed in Australia on a pension under the double tax agreement, but not in the UK. Often with corporate pension plans in the UK, to start a pension they actually go and transfer it out into a different fund to acquire an annuity. Technically, that would trigger 27CAA. I think it is fair to say that it does not seem to be administered that way. The Australian Tax Office is not hot on the heels on trying to pick these up, but technically that is the way 27CAA could operate.

Another technical problem with 27CAA is when you are dealing with defined benefit funds overseas. The way you do a calculation to work out the taxable amount in 27CAA deals with contributions and a few terms in there which are difficult to translate with certain types of funds which may be in surplus so there are no contributions. I will not go into all the detail on that,

but time and time again we have come across having to ask questions of UK pension funds to get dollar figures to work out 27CAA liabilities for clients. They cannot give the answers because the information that is needed is not actually consistent with the way a fund is run over there.

Senator HOGG—Are you saying these are technical difficulties—

Mr Forsdick—Existing difficulties.

Senator HOGG—because no-one has sought to try them or test them at this stage, or has someone?

Mr Forsdick—Not as far as I know.

Senator HOGG—I presume it would be the Australian—

Mr Forsdick—Just poor wording of the legislation. It does not really recognise how pension funds and overseas funds work. Can I give one more example of the technical difficulty?

Senator HOGG—Yes.

Mr Forsdick—With the way 27CAA is worded, let us say I was working in London for a multinational and I joined in 1977. I worked there for three years and I was in their pension plan. I came out to Australia to work for the subsidiary for a couple of years in the late 1970s. I worked here for a couple of years and continued membership of that plan. I then go back to the UK in mid-1985. I love this place so much that I come out here 15 years later to work here, but I get my benefit transferred out here. The 27CAA tax is backdated from the time I first came to Australia back in the 1970s. I would theoretically, under 27CAA, have to pay tax on the growth in value, excluding contributions in all that time. That is just crazy. Those are some of the particular technical difficulties with 27CAA, and hence our interest in the submission. There are some easier alternatives, which can accommodate the needs of the people who transfer over here and are much better than the existing regime.

CHAIR—We are still dealing with the problems of section 27CAA. A witness earlier today indicated that there is no legislative requirement to provide a credit in respect of the interaction of 27CAA and the FIF taxation regime. Is that correct? You generally get a credit, I understand, but there is no legislative provision for it.

Mr Forsdick—I believe that is right. I do not think there is any specific provision which enables that to happen. That is something I would need to double-check.

CHAIR—Yes, if you would not mind.

Mr Forsdick—Of course the FIF regime is often an incentive for people to bring money out here because if they have a personal pension plan in the UK then they are paying tax as it grows with no cash. In my experience we have not had an issue of double taxation on that. But that does not mean that would not happen, of course.

CHAIR—You indicated that sometimes funds in the UK have difficulty in understanding the terminology and making the necessary calculations. An earlier witness today suggested there was just some outright reluctance to even provide the necessary information whether they can provide it or not. Have you come across that?

Mr Forsdick—It is difficult sometimes to make that judgment.

CHAIR—They are just not interested.

Mr Forsdick—We have generally managed to achieve transfers. The hurdle is at the UK end in getting the approval.

CHAIR—This was certainly the American example within a global company—there is just that reluctance by the fund managers in the United States to provide the information.

Mr Forsdick—I would not say that we have really come across that. When you are looking at US payments on, say, 401K plans then there are particular tax consequences in the US anyway, and penal rates of tax if you are under a certain age, and so on. I would not say reluctance; I have not had an experience of reluctance. I suppose I have had an experience of a fund being not interested in helping it move along very quickly, but not obstruction in any way.

CHAIR—Do you think there would be any difficulty in getting the UK revenue authorities to change their mind to enable a deduction to be made either by the fund or the individual in terms of transfers across? Or would it take an international agreement to make that possible?

Mr Forsdick—I would think it would take an international agreement. If you were going to go down that path, I think 27CAA is just one part of a range of issues to do with people who move between countries or emigrate and deal with retirement benefits. 27CAA is just one element. There are a number of interplays, which can result in double taxation. I think the only solution to those problems is individual agreements with countries. That is the problem with 27CAA, it is a sort of catch-all provision on everything when these things are probably best dealt with through double tax agreements and bilateral social security agreements.

CHAIR—Have you had any experience with any of these?

Mr Forsdick—I know that the US and the UK bilateral social security agreements were being renegotiated. I am not quite sure where that is up to at the moment. These have always tended to deal with pensions, not lump sums, and the double tax agreements only ever deal with pensions. At this stage we do not have any agreements which will deal with this transfer of benefits in a proper and complete way.

CHAIR—Do you think that if the Australian regime moved to an income streams approach it would facilitate payments? Is it the lump sum mentality that makes people overseas have some reluctance to transfer money?

Mr Forsdick—I have not had any experience of that. As I said, I have not had any experience of difficulties in getting transfers through, for any reasons other than perhaps red tape in the overseas country. Take UK as an example, you can receive lump sum payments in

the UK of up to 25 per cent of your benefits. It is true that Australia may have a lump sum mentality, which I think is changing anyway, but US and UK pay lump sums too.

Senator ALLISON—On the question of the relevant day, under your third option, how and when would that be determined? In terms of the process, given that you might have a range of dates of starting and stopping work in this country and becoming a tax resident and not, where do you see the business of determining the relevant day being made?

Mr Forsdick—First of all, it would be very difficult to impose that on the overseas fund so I think it is going to have to be done through a self-assessment calculation. When you look at any of these options, the super fund here, in some ways—if it is going to accept the transfer from overseas—is going to have to get information from the member of the fund so that the proper calculations can be done. It would have to be reefed back to the individual to provide that information. Obviously, they have a clear responsibility to provide the correct information. I think that is the only way that it could be done.

Senator ALLISON—I am still not sure what you think about relevant day. Is it the first day of the continuous employment in Australia leading up to retirement? At what point can you know that? Will you not know it until you retire?

Mr Forsdick—If I go back to the principle that what should only fall in to be taxed here is any growth in benefits whilst an Australian resident, the relevant day method provides a starting point and everything after that date gets caught. Where you have broken periods of service, it should recognise those broken periods of service. In the example I gave, the receiving fund would have to treat the amounts which relate to the period of service in Australia as whichever option you choose, as either a taxable or an untaxed element. So you do away with relevant day and you are just dealing with periods of residency here in Australia. Obviously, that would introduce some complexity, but it has a better chance of being fair.

Senator ALLISON—In terms of flexibility, you suggest that option 3 is administratively simpler. How would that 15 per cent higher tax be applied where the money was brought into a pension fund? Would you do it weekly, monthly or whenever the payments were made?

Mr Forsdick—In option 3 the tax is payable at the end when the benefit is paid out. The super fund would have to record this as a special component in the benefits. There are a number of components that comprise super benefits at the moment. The super fund would have to have a component which would be taxed when it is paid out—rather like an untaxed element is currently taxed which is at a 15 per cent higher rate. That amount, whatever that dollar figure is, is recorded by the fund in the same way that undeducted contributions are recorded. When it ultimately gets paid out, it is taxed as an untaxed element. This means, if it is a lump sum, that it is taxed at 31.5 per cent or, if it is paid as a pension, that it is a non-rebatable pension so it has no 15 per cent tax rebate.

CHAIR—By the time you pay tax to get it here and pay tax on the end benefit, if you take it as a lump sum, it is a fairly high rate of tax that is applicable, is it not?

Mr Forsdick—Is that a comment on the way that superannuation is generally taxed in this country or is that a comment on that particular construct?

CHAIR—I am seeking your views on that. An earlier witness indicated that we are moving to a situation in Australia now where the taxes on superannuation are much higher in some cases than their own personal marginal rates.

Mr Forsdick—Yes. I have come across an instance where, as a result of a retrenchment payment, the effective overall tax rate was over 85 per cent. And this is for somebody who was actually retrenched. There are a lot of hidden taxes and consequences which may happen some years down the track with reasonable benefit limits and so on. I applaud the government's initiative to limit the tax on benefits, to limit the effective tax rate on the excessive amount of superannuation payments—presumably to no more than 48½ per cent—which was announced on 5 November and also in the budget papers last week. I think that is good because that will really help solve a lot of the problems that the people I refer to—and you refer to—are facing. The issue that is going to be there is how one ever achieves that through administration, because, if you are going to limit the end benefit tax, you have to work out what tax has been paid in getting there. That is anywhere between zero and 30 per cent, and super funds are not tracking that. So I think that it is an initiative to be applauded. I just think it is going to be very difficult to work out a solution to it. But we are in a country where we tax at three points, which is very much out of step with the rest of the world. Our firm, and I think a number of people, would like to move towards the taxing of end benefits.

CHAIR—We had that previously.

Mr Forsdick—Yes, that is right. Given the level of revenue that is currently taken from superannuation funds in the surcharge and so on, that clearly would have a major impact on the budget. So we would have to do it—and I suppose there has been a start, hopefully. That is going to take a while. But we need to inexorably move—in a staged program so it does not create too much stress on the budget—towards the taxing of end benefits. The key benefit of that is that the government of the day would be getting revenue from benefits at the time when it needs it the most, if you read the Intergenerational Report.

Senator ALLISON—With regard to the tax at the end and how you work out relevant days and so on, if we treat the transfer as an untaxed element, why would you need to bother about time frames at all—or even periods of residency?

Mr Forsdick—I am not suggesting that the whole of the transfer is treated as an untaxed element. I am just suggesting the 27CAA amount—

Senator Allison—The growth.

Mr Forsdick—Yes, the growth. This is getting back to the principle that any amounts which did not relate to Australian service, or have been taxed in some other way—which is why contributions are excluded from the calculation, because either they have not been deductible to the employer or they have been subject to fringe benefits tax while people have been here. It is only the earnings component that is otherwise untaxed.

Senator BUCKLAND—Apart from the difficulties that you face with tax in this 27CAA that we have been hearing about all day, what other impediments exist that complicate transferring funds into Australia?

Mr Forsdick—I would say from an Australian perspective the superannuation system here is quite malleable. I do not see any impediments here in Australia. It is usually getting the approval from overseas for the transfer to occur. In getting those approvals, those overseas authorities generally want to get a bit of an understanding of the Australian system to make sure that an Australian superannuation fund is a bona fide superannuation fund in their eyes. With preservation and the rules we have on loans or not being allowed to have loans, and on early access and so on, it stands up pretty well to scrutiny. In my experience, the aspect of being able to get hold of a lump sum has not made people overseas say, 'This is not a proper superannuation fund.'

I do not think there is anything in the Australian system that is acting as an impediment, other than this tax issue. It is more the overseas regimes, where there are strict rules, and also the way overseas regimes tax superannuation. For example, if you are a US citizen working here, you still pay tax in the US—you are effectively a tax resident of the US as long as you are a citizen. The US authorities do not recognise Australian superannuation funds for US tax purposes. So a US person working here and having contributions going into the fund under a super guarantee or whatever and having earnings in the fund, have to return, in their US return, those contributions and those earnings and have to pay US tax on it. I do not see that as a fault of the Australian system.

Senator BUCKLAND—No, that is not a problem. That is something they have to deal with.

Mr Forsdick—But those tend to be the issues.

Senator BUCKLAND—There is a difficulty with some funds not accepting contributions from overseas funds, is there not?

Mr Forsdick—I have not had a problem with that. To get the release from overseas funds there are some procedures that you have to go through with the overseas authorities and some funds here in Australia. I have had difficulty with the overseas authorities accepting the fund here in Australia as being a bona fide fund for transfer to a personal superannuation fund where you are the trustee. In the UK, they look at that and think, 'Well ....', because that does not happen so much in the UK. But, again, I do not see that as a problem with the system here; it is just overseas getting an understanding of our system.

Senator BUCKLAND—In your dealings with fund transfers and superannuation over the years—and I imagine there are a few years experience there—have you found that there is greater difficulty for people from any country who make their own determination that they will migrate and come to Australia as opposed to those who are, if you like, sponsored out here by the corporation or the company decision to transfer them? Is there a difference? Is it more difficult for one than the other?

Mr Forsdick—I would say the answer to that is: no, not on that basis. We do, however, find it easier to deal with corporate plans overseas rather than a life office or a personal arrangement or whatever, because the corporate plans tend to be more understanding if it is related to an employment transfer. They may have more experience of it if it is a corporate plan for a multinational. They may speak to their HR department or the HR department may oil the wheels to speed up the transfer. I think it is fair to say that we have found it easier to make it

happen with corporate plans than non-corporate plans overseas. But I do not see that difference being as a result of what you said.

Senator BUCKLAND—This morning we touched on the question of information being available to people. From where I sit, it would seem to me that there would be more information available to those who are being transferred by the corporation, and they would make all of those arrangements. In fact, we had evidence this morning that the witness was provided with accounting services to do exactly that—to advise them of what implications were there. Where would someone who is just deciding that the family will now come and live in Australia get the information about all of these difficulties?

Mr Forsdick—I would say that the ability to do that is not well known publicly. I think it has become more publicly known, but I would expect that many accountants and advisers, even in Australia, until fairly recently really would not have known very much about the ability to do that. It is an initiative that is not taken over in the UK, for example, by the life office or whatever to say to people, 'You've gone to Australia; you can transfer your money'; whereas, with corporates, it may be just part of the overall transfer package to say, 'We'll help facilitate that.' So I cannot really answer your question. I suppose speaking to a professional adviser will give you an idea that you can do that.

CHAIR—Mr Forsdick, as there are no further questions, I thank you very much for appearing before the committee.

[2.00 p.m.]

ELLIS, Mr Paul Anthony, Principal, Human Capital, Andersen

CHAIR—Welcome. We assure you that you are protected by parliamentary privilege, and you do have the opportunity to make a request to the committee to give any of your evidence in private and we will consider your request.

Mr Ellis—Thank you. To give you some background, our practice deals mainly with expatriates and people coming to and from Australia, and international pension and superannuation issues. That is the background that I am coming from. I am not a superannuation expert as such—I do not deal every day with all the wide provisions of superannuation but I do deal extensively with 27CAA and the implications of moving superannuation amounts into Australia.

To reiterate, under the current rules, unless you remit your overseas superannuation to Australia within six months of arrival you will pay tax on the growth in those moneys at 48.5 per cent. Our concern is that that can result in very high effective tax rates when comparing the total foreign tax and Australian tax that is paid with the tax payable on retirement benefits generally in Australia. If you look at the example we have set out in our submission, the case of someone transferring money from a 401K plan in the US to Australia results in an effective tax rate of nearly 43 per cent compared with a rate of 31.5 per cent that we more commonly apply in relation to Australian superannuation benefits. There is a significant high level of taxation which is a disincentive, if you like, for those moneys to be moved to Australia.

I would like to comment on one of the proposals that was discussed in the session just before this. In relation to the first two proposals from PricewaterhouseCoopers involving the fund paying the tax and the tax being remitted into Australia, the difficulty with those proposals is that, as the law is currently drafted, if you do that the fund would not be entitled to claim a credit for the tax that is paid overseas—in the US, for example, or in Singapore, if it is coming out of a private pension plan there. So you could actually end up with a higher effective tax rate again because you would still pay the foreign country tax and then you would pay a further 47 per cent or 15 per cent tax here plus possibly some tax—another 15 per cent—when the benefits are taken. You could end up with higher levels of taxation on the total benefits received at retirement.

CHAIR—I think we acknowledge that if you went down that track the provisions would have to include the credit.

Mr Ellis—Absolutely. I wanted to make sure that that was the case. That is a significant problem in terms of the total effective tax rates. In particular, looking at the way the six-month window operates under 27CAA, the problems that we see are that in many cases it may not be possible to get benefits released from a foreign country. For example, Canada is one country where it is not possible for benefits to be released until retirement age. They have a preservation system similar to the one we have had in place here, although that will change from 1 July.

Also, it can be quite difficult from an administrative perspective. Some administrative difficulties have already been mentioned by the previous witness, such as how it can take time to get information and the like and that, therefore, six months may not be enough. In other

situations a penalty tax applies in the foreign country—for example, in the US—if you take the money out before retirement age.

Finally, the biggest difficulty that I tend to come across with the way the six-month rule operates is with people who originally come here on temporary residency visas. They may intend to stay for six months, two years, three years or whatever but decide they like the country and want to stay permanently. By the time they know that they want to stay permanently and they have made the decision that this is where their retirement benefits probably should be, it is too late to take advantage of that provision because the six months have expired already.

Three guiding principles have been used in formulating the proposals in our submission. One is that we want to encourage the early transfer of offshore retirement funds to Australia, because it is good for the Australian economy. We also want to encourage the preservation of those amounts as retirement savings. Under the present rules, the tax applies whether you take the money in cash and spend it or whether it goes into a fund. The concessions proposed in our submission would only apply where the money goes into a fund. So if you take the money and cash it out, then you still pay the tax as per the current rules.

Finally, we are trying to provide a more comparable treatment to the way in which Australian retirement savings are taxed. Again, I would just like to make a comment on some of the earlier discussion in the previous session about how that might be achieved. In my view, to leave the taxation or such a position to individual negotiation under international tax agreements or under bilateral social security agreements is a dangerous way of going about it. You end up in a situation where people will be taxed in different ways, depending on which country they come from and whether Australia has been able to negotiate some sort of arrangement. Effectively, you end up with a real hotchpotch of different treatments. However, under the proposals that we have set out, you at least get an equality of treatment, irrespective of where the person has come from.

Under our first proposal, we try to address the high effective tax rates. We suggest that any transfer to a complying fund in Australia from an overseas fund, where that money has been subject to overseas tax, should be treated as an undeducted contribution going into a fund in Australia. Our basis for suggesting this is that the money has been subject to a comparable tax in the overseas country and, therefore, it should be treated in exactly the same way as any after-tax contribution in Australia. That is, the money goes in, it is not subject to contribution tax, it is not subject to exit tax, but the income that accumulates from that money being invested is taxed in the normal way.

As long as overseas tax has been paid in the foreign country, there is no reason, in principle, why the treatment should not essentially be the same. Someone coming out of the US or Canada at retirement time or out of Singapore with a private pension, for example, would end up being treated in the same way as someone in Australia having made contributions from after-tax income. There may be some minor differences in the actual tax that is payable in the foreign country compared with Australia. Again, going back and looking at the example in our submission, the actual or incremental revenue generated in Australia, even at the 48½ per cent tax rate, is not that significant. So that is our suggestion where tax is being paid in the foreign country.

CHAIR—Are you suggesting that neither the capital gains tax nor the 15 per cent nor the marginal tax rate should apply?

Mr Ellis—That is right, because essentially that money is like any other money that has already been earned and taxed. If you or I or anybody else takes money that we have paid our tax on and puts it into a superannuation fund then that is how it is taxed, because we have already paid our tax. In the same way, if you take money out of a foreign system and you have paid tax in the foreign country, as long as that tax is comparable why should we seek to tax it again? You have paid your economic share of tax, if you like, and it should be treated in exactly the same way as an Australian's after tax contribution would be treated.

CHAIR—The phrase 'in a comparable tax country' is notable because I can see situations where it could be used to accumulate lots of capital and then get that transferred at minimum tax rates.

Mr Ellis—I acknowledge that and therefore some work would need to be done to define a list of countries from which it would be acceptable. That has already been done in lots of other contexts.

CHAIR—Such as the list from the FIF rules?

Mr Ellis—Exactly. I think you would need to do some work. For example, as we have already heard, you can transfer money from the UK and there is no tax in the UK if you can satisfy the UK rules. Under the scenarios where that is the case, we are suggesting that you allow it to be rolled over as a taxed contribution—in the same way as a rollover from any other fund in Australia, in effect. There is some benefit there, in that you have not paid the 15 per cent tax, but that is the incentive to bring your retirement saving to Australia from a white listed country. So that would not apply, for example, if the money were coming from Hong Kong, Jersey—the Channel Islands—or any of those tax haven type countries.

CHAIR—What tax rate are you suggesting should apply to those other countries outside the list?

Mr Ellis—Just the same treatment as currently applies.

CHAIR—The full marginal rate?

Mr Ellis—Yes. My view is that we should not provide concessions where people have been accumulating money in tax havens. But by far the vast majority of the people that I see and deal with are people who come from our major trading nations and whose retirement moneys have been accumulated in funds in those locations—the US, Europe, the UK and Canada. They are coming from genuine retirement funds where it is rare that the moneys can be accumulated and taken out without paying some tax in that country. The UK is perhaps the only example that I am aware of, because of the particular way in which that system works. If you address that by allowing a rollover as a taxed contribution, you can achieve an equitable result. So what you would do is effectively allow a rollover for the post-residency growth piece, but the pre-residency piece should also be treated as an undeducted contribution for the same reason as the other.

CHAIR—So the whole lot would be treated like that?

Mr Ellis—There would actually be two different bits of it: the pre-residency bit, as now, would be tax free and treated as an undeducted contribution, which is exactly the same treatment as applies now; the post-residency growth would be treated as a taxed contribution rollover.

CHAIR—As a taxed contribution?

Mr Ellis—Yes.

CHAIR—Why separate the two, according to your philosophy?

Mr Ellis—Because at the moment if you take what you have at the time you arrive here, there is no further tax on that. If you put it into a fund, you only pay tax on the income, not the capital piece, and you do not pay any tax when it comes out. So essentially the money you have when you arrive here is treated as your money with no further tax to pay. What I am suggesting is not going to change that, so that piece will remain the same. It is just the post-residency growth piece that 27CAA currently applies to. So that is our proposal to address the tax rate problem.

I think there are also a number of problems with the six-month rule. The second proposal in our submission suggests that we extend to two years the six months that currently apply. That is simply to provide additional time so that, where there are administrative problems or—as was alluded to in the previous session—where the person may not know, because they do not have access to professional advice immediately, it gives them some time to discover and to act without being subject to the six-month period, which tends in practice to be somewhat restrictive.

The second element that we are proposing—and this is important for people who come here originally on a temporary residency visa—is that the operation of 27CAA only commences from the time that a person becomes a permanent resident. That gives people some time to address whether or not they are going to be here temporarily or permanently. If they do decide to stay here permanently and therefore they need to think about having retirement benefits here, then they have the opportunity to benefit from the 27CAA principle without being penalised because they have been here for six months. We see that as being not an alternative to proposal 1 but in addition to it. It gives people a window either to take the money if they can or to decide to act under proposal 1.

The other point to note which is not addressed in our submission is that, although there was some discussion of the foreign investment fund or FIF rules earlier, those rules will only apply where the money is kept in a private superannuation or private pension arrangement rather than an employer sponsored one. But where they do apply, there is a battle between an individual potentially having to pay tax under the FIF regime or, if they bring their superannuation to Australia, having to pay additional tax at high rates, as we have already identified. As noted in the earlier session, the question is whether or not you can claim a credit for the tax paid under the foreign investment fund regime.

Our third proposal is to confirm that the transfers that come from overseas within that six-month window are treated as undeducted contributions. That is the practice at the moment, but there is some uncertainty within the legislation, from a technical perspective, as to whether that in fact should be the case. If nothing else happens, we recommend that that treatment be confirmed.

Finally, although it is perhaps beyond the brief of the committee today—which is to look at 27CAA—if we are looking at the interaction of foreign and Australian retirement benefits, it behoves us to also consider the treatment of pensions. People who cannot or do not access their foreign retirement benefits because of the problems we have already identified, and who then take them as pensions when they reach retirement age, are significantly disadvantaged under the current law compared to people who are taking a pension from a complying fund in Australia. This is because they do not have access to the 15 per cent rebate regime, and it is questionable whether they also have access to the undeducted contribution deduction.

Senator ALLISON—Could you step us through the illustration concerning someone who migrates from the United States, on page 2 of your submission? I am not sure I understand how this works or where the calculation against growth occurs. I wonder, in the case of the US—where there is such a big tax take—whether that would be a reduction rather than a growth. I do not know how that fits with the current rule.

Mr Ellis—I will address that last point first. The way in which 27CAA works is that it applies to the gross amount that comes out of the fund, not the after tax amount. So whatever you withdraw from, say, the 401K plan in the US—in this case $160,000—is the amount that is subject to the operation of 27CAA. What we are saying in this example is that $50,000 of that $160,000 represents growth since the time they have become a resident. So they take $160,000, and for US tax we have assumed tax at 30 per cent as a fair enough median—it may in fact be higher than that, depending on the individual's marginal tax rate and the operation of the 10 per cent penalty tax. There is an extra 10 per cent tax there: it is $48,000 at 30 per cent, plus the penalty tax, and so you pay $64,000 in tax and you are left with $96,000 to bring to Australia. Of that $96,000, $50,000 is subject to tax here—that is the post-residency growth. The prima facie tax on that, at 48½ per cent, is $24,250. You can claim a foreign tax credit. Again, we have only claimed the credit that relates to the piece that is taxed in Australia; we have applied, in effect, a proportion to the $50,000 and claimed that. So the incremental tax in Australia is $4,250, and that is an effective tax rate of nearly 43 per cent on the total payment.

Senator ALLISON—But it is not a 43 per cent Australian tax, is it? It is combined.

Mr Ellis—No, definitely not. What we are trying to do is to demonstrate the total tax burden that applies. That will vary from country to country.

Senator ALLISON—This individual would have more argument with the US government, though, than with the Australian government in this arrangement.

Mr Ellis—I guess they would but, if you take out the incremental Australian tax, that brings you down to a rate of something closer to 35 or 36 per cent, which is acceptable in the context of the American regime. In our context, it is higher than you would pay in Australia, but if there were no further tax in Australia it would probably still be just acceptable; it is the price you pay

for getting the money out of the US regime and into Australia. But, when you combine the two, you can see that the extra $4,000-odd of tax makes for an additional impost that has an impact on the tax rate.

Senator ALLISON—How is that 30 per cent applied? Would this be a pension fund, or is that just applied to the lump sum in the US?

Mr Ellis—It is a lump sum. In the US, the money that comes out of a retirement fund is taxed as ordinary income. That is why that sort of rate is more acceptable in the US context: because you have pre-tax contributions subject to limits and you have no tax in the fund and so the only tax you have to pay is when the money comes out—but you do pay tax as ordinary income at whatever the applicable marginal tax rates are.

CHAIR—On the second-last page of your submission, under the heading 'Related issues', it says:

Pensions paid from foreign funds are not entitled to receive the 15% rebate available in respect of pensions paid from complying ... funds.

Isn't it true that pensions from, say, the UK, attract a deduction equal to eight per cent?

Mr Ellis—Not that I am aware of.

CHAIR—This recognises the personal contributions that they may well have put into the fund, without going into the details of it.

Mr Ellis—I was not aware of that. It may be that some people have been able to get that sort of practical result in negotiation with the tax office, but I am not aware of a general policy.

CHAIR—I just thought I would draw your attention to that one, in addition to making that point. Thank you very much for speaking to us, Mr Ellis.

HUTTON, Mr Steven Brent, Director, Pension Transfers Direct Pty Ltd

CHAIR—Thank you, Mr Hutton, for appearing before the committee, today. You are protected by parliamentary privilege and should you make a request to the committee that some aspects of your presentation or what you say be taken in private, we will consider your request.

Mr Hutton—I am a director of Pension Transfers Direct Pty Ltd. I am also an authorised representative of Associated Planners Financial Services and an associate member of the Financial Planning Association of Australia. I have been in the industry for 15 years.

Pension Transfers Direct commenced business in 1997 and our challenge was to bring some public awareness to what we refer to as the 'sleeping giant'—this section 27CAA. Over the ensuing five years we have transferred approximately 600 pension funds from the UK. More importantly in light of this review, we have spoken to probably in excess of 2,000 other migrants or returning Australians who have not acted to transfer—the overwhelming reason being that they did not want to trigger this section 27CAA. For all intents and purposes, they have put their heads in the sand in the hope that it goes away over time—particularly those who have residency dates prior to 1 July 1994. This touches on retrospectivity and the fairness of that.

I will talk to the submission we have made. Firstly, with regard to the retrospectivity, the legislation was passed on 1 July 1994 but is effectively backdated to the date the person became an Australian resident. We have spoken to many migrants to this country who arrived in the late seventies, early eighties and mid-eighties. By the time we spoke to them about this issue, they were sitting on quite a large contingent tax liability, through no fault of their own. Many of them are very upset that they were not in a position when they arrived, prior to 1 July 1994, to make an intelligent decision as to the best course of events for their pension funds. We deal primarily with the UK. I believe the retrospectivity is un-Australian and unfair. Our first proposal would be to remove the retrospectivity. The tax treatment of the growth should commence either at 1 July 1994 or at their date of residency, whichever is the latter.

CHAIR—Before you go on—and as we have the representative from Andersen with us—you make the point that, in addition to the tax rate, classification of the growth in funds transferred as assessable income also affects the superannuation surcharge.

Mr Hutton—Yes, that is right. It is again one of those technicalities referred to by an earlier witness: it is personal income and therefore it is assessed as part of their adjustable taxable income when calculating their rate of surcharge. It also counts towards their taxable income with regard to the Medicare levy surcharge and Centrelink benefits. We have many clients, particularly female clients, who have unfortunately been through separations and are relying on Centrelink benefits. If they were to trigger this tax, they would lose those benefits and, potentially, have to repay what has already been paid to them.

CHAIR—I am sorry to interrupt, but I think you are the first witness who has raised this issue with us. That is why I wanted to verify it in the presence of others who may have had similar experience.

Mr Hutton—One of the earlier transfers that we did caught us unaware and the knock-on impact of this assessable income under section 27CAA is now part of our report and analysis to these clients.

Senator HOGG—You are saying that they would get assessed under section 27CAA and pay 48½c in the dollar and on top of that there would be a further assessment for the surcharge?

Mr Hutton—Yes, it is personal income.

Senator HOGG—As personal income?

Mr Hutton—Yes.

Senator HOGG—What does that lift their rate to?

Mr Hutton—From the point of view of the surcharge, many people we deal with fortunately are already beyond the top limit anyway, earning over $103,000, so it has no impact. But unfortunately for many people, particularly in Perth and South Australia where average incomes are a bit lower, this assessable income generated by way of a transfer will often put them up into surcharge country, trip them over the $88,000 it is now.

CHAIR—One of the reasons for one witness to come before us was the case of a lady who worked in the retail area on quite a modest income. Quite a modest amount went in but because of the exchange rate and other issues the growth was very significant. So, from a very small income, this lady would be catapulted into the surcharge regions and be paying quite a hefty surcharge even though she would have no other surchargeable amounts.

Mr Hutton—Certainly. And the same could be said for people on Centrelink benefits, where it would put them up over the threshold.

CHAIR—Of course. They could lose their Centrelink benefit.

Mr Hutton—Or, more difficultly, they would have to repay what they have already received—which has been the case.

Senator HOGG—Would this also affect people who are paying child support?

Mr Hutton—My understanding is yes.

CHAIR—You are suggesting that a person can not only be subject to the surcharge but also be unable to access the money. I suppose they could access it for surcharge purposes because the legislation enables them to access it for surcharge purposes. So that could be deducted by the fund, I presume, because the individual doesn't pay that.

Mr Hutton—It depends on which fund the money is going into. You will find that, with the restrictions and technicalities that have been touched on earlier, not many Australian funds will take on the responsibility of the transfer from the UK.

CHAIR—Not many funds will?

Mr Hutton—There are certain criteria that have been relaxed post 5 April—the recent UK budget. But prior to that, if for example it was coming from a personal pension plan in the UK and the transfer value was greater than about £22,000 there would have to have been an undertaking from the Australian trustee, the receiving scheme, to pay the majority of the benefit as a complying annuity. With most Australian trustees, it is still that lump sum attitude that we are talking about, where the client at retirement has the choice of taking a lump sum and/or a pension. He has no right to implement that compulsion to take an annuity, which is one of the reasons that this process has been difficult. Earlier, we touched on the question of UK reluctance or Australian problems in receiving the money. That is one of the issues: quite often the UK fund will want the Australian trustee to mirror the rules and regulations of the UK fund to let that money go. As I said, that has since been relaxed but that was certainly a major obstacle in the past.

CHAIR—You have just raised some interesting points. Continue.

Mr Hutton—From experience and from talking to many migrants, the six-month grace period is not practical. There are more important issues than their pension fund—namely employment, housing, children’s schooling and the simple fact that they are not sure they are committed to staying. Six months is not a long time to decide that Australia is the place where they are going to live for the rest of their life. The other issue I mentioned earlier is fighting the paper warfare with the UK funds and regulators. It can quite often take several months, depending on the efficiencies or inefficiencies of the UK scheme involved. The other problem—and again, this has been our challenge—is to raise awareness. Most of them are blissfully ignorant when they arrive in Australia. There is no form of education that we know of prior to their leaving, in terms of addressing the issue sooner rather than later when they get here.

Senator HOGG—Can I just ask about the paper warfare that you referred to. Surely in today’s era of modern communications, with emails and the like, there are a lot of barriers broken down?

Mr Hutton—Yes, there have been, and also the volume of paperwork has been reduced considerably, certainly over the last five years that we have been specialising in this business. A lot of that has been driven by our communicating with the authorities in the UK. David Ford, our managing director, is in the UK at the moment and will be meeting with them. So it has been a communication procedure. I know for a fact that in the early days one of the problems they saw was that there was this loophole under the Australian superannuation legislation where if an Australian resident hand on heart was leaving Australia permanently for overseas then he could encash his benefits. I think that was being abused in some cases where people would come to Australia, effect a transfer from the UK and then return to the UK, hand on heart leaving Australia permanently, and end up with the cash in the hand. Just the general lump sum history of the Australian scheme I think was an offputting experience for the UK. But basically a migrant still needs to prove to the UK trustee that he no longer has any employment ties in the UK, he is employed in Australia and the superannuation fund in Australia is complying and is also a resident in Australia. That sounds pretty simple, but unfortunately it can take some time.

CHAIR—Coming back to the earlier case, we could have a person who is on, say, some sort of government benefit, a disability pension or something like that, and he gets this wallop of income. He has not gone to a professional adviser, he has made the request, the money has been transferred and has gone into his fund. He then gets a huge tax bill included as assessable income and pays the surcharge. Social Security get to know that this is income and he loses the pension. He also has to pay higher child support, and he has got no income. So he has got no income that he can access from the overseas payment, he loses his government pension or some other benefit and is up for a high child support payment.

Mr Hutton—Yes, it is frightening, isn't it?

CHAIR—The mind boggles at the tax consequences just because a person thought he would bring the money in without getting good advice and the fund agrees to it. He is up for these taxes, losses of benefit and added responsibilities.

Mr Hutton—From practical experience that is the very reason that people will put their heads in the sand and hopes it goes away. Why would they trigger that?

CHAIR—Yes.

Mr Hutton—I made some notes from one of the early witnesses as well. The question was asked with regard to identifying the residency value, the historic value, as to when this growth starts. Obviously the difference between that and today's current transfer value is the growth that is assessed. We actually assisted a client in Perth with seeking an opinion from the ATO because indeed many of the funds we are dealing with are defined benefit final salary promise type schemes and, when we request the transfer value as at 1 July 1998, many of them will come back and say, 'We don't have it. It is irrelevant. Why do you need it?' This particular fund would not give us any information so we wrote to the ATO, or the client and his accountant did, asking for an opinion. The ATO responded with some written advice saying that unless the historic transfer value was identified they would treat the whole lot as growth and assess the whole lot as income.

Senator HOGG—Can you get hold of a copy of that letter for us? Expunge the name for privacy reasons. I think that would be an interesting item to have tabled before the committee.

CHAIR—And not only the name but any numbering or lettering or file number.

Senator HOGG—Anything that can identify it.

Mr Hutton—They actually declined to give the opinion or the ruling—

CHAIR—Even the geographic source of the tax office.

Mr Hutton—They basically stated to the client that, in the spirit of the legislation, he needs to identify it. They would not accept that there has not been any nominal growth, and in the spirit of 27CAA he had to provide a fair figure—which was a challenge in itself for the client and his accountant.

Senator HOGG—Is that what they call creative accounting?

Mr Hutton—Yes—billable hours as well, I believe. With these sorts of issues, you can see that six months is just unrealistic. We believe a critical first step is to provide the client with a written analysis of what they are holding in the UK. Unfortunately, many are not aware of the benefits held in the UK. Before transferring, we make sure they understand exactly what they have in the UK and also the comparative tax issues. Generally, it will then end up with their accountant and that adds further time to the process.

With regard to bringing the money into Australia, obviously there is the 15 per cent revenue, the tax on the earnings in the Australian fund. We believe this is the basis of the change to the existing section 27CAA, and we fail to see the logic on why it is a personal income tax. If the client had transferred the money into an Australian fund prior to 1 July 1994, the maximum rate of tax they would pay on earnings is 15 per cent, and that is often reduced with franking credits and imputation credits if they are investing in Australian shares. Our proposal for 27CAA would be that the growth only starts post 1 July 1994 and that the amount identified as growth is deemed to be an untaxed element on transfer; that the balance is, as it is today, received as an undeducted contribution but the growth component identified as an untaxed element and taxed at 15 per cent upon receipt of the fund, as an untaxed or unfunded element is today from a public sector or a golden handshake from an employer. We do not see that it needs to be any harder than that.

CHAIR—I would like to congratulate you on the table that you have presented to the committee. It is very clear. It is a very good presentation.

Mr Hutton—Thank you. It is the sort of format we use with clients. It is a bit more concise.

CHAIR—It is excellent.

Senator HOGG—I am interested in the fact that you said that you had canvassed some 2,000 migrants on this issue over a number of years, I would presume.

Mr Hutton—Yes, over about five years.

Senator HOGG—Have you made representations anywhere in that five-year period to try to have the problem addressed?

Mr Hutton—Yes, we have—and I believe he was your first witness this morning. We have encouraged clients to go back through their own local federal members. One of our inquirees was a witness earlier this morning, and I believe he has been quite active. He is in Mr Hockey's constituency. I believe we have had several people who are more motivated than others to pursue the issue.

Senator HOGG—The reason I am asking is not to cast aspersions on your or your organisation; it just seems to me that it has taken a long time to get any momentum. It was a colleague of ours in the Senate who wrote to the committee seeking that the committee inquire into this matter. It did not seem as though there was any concerted approach.

Mr Hutton—We wrote several times, particularly in the first couple of years of trading when some these other knock-on effects were coming to light, and generally received some pretty abrupt replies.

Senator HOGG—‘Get lost’?

Mr Hutton—Effectively.

Senator HOGG—Can you give us some sort of profile of the 2,000 people? Are they mainly professional people? Are they mainly high income earners? In the case that Senator Watson referred to that basically triggered the inquiry itself, there is a fairly low income earner who has a fund that, through exchange rate changes and appreciation, has appreciated quite substantially in the UK. Can you give us a feel for the type of people we are looking at?

Mr Hutton—Our research is showing that eight per cent of the Australian population is UK migrants. As you can imagine, there is quite a wide range of people and personalities. Particularly in the last few years, it has become more and more difficult for these people to get Australian residency. They have to jump through all sorts of rings and hoops and the point system to get here, and a lot will depend on the trade, profession or skill that they hold and what they can offer the country. So, generally speaking, they are professionals. For example, in Western Australia there are a lot of people in the oil and gas industry with what is happening up there in the shelf; in Sydney, we see a lot of IT, accounting and legal people; in Queensland, particularly in the eighties, there were a lot of teachers heading up to Brisbane; and the common theme is probably the medical professions, as there are a lot of doctors, dentists and nurses.

Senator HOGG—So there are a range of professions and a range of incomes. One would presume that the majority of these people are not necessarily coming out as permanent residents in the first instance.

Mr Hutton—That is true.

Senator HOGG—They would be coming out for a prescriptive period of time and then either going back to the UK or finding that they have had an offer too good to refuse and are staying.

Mr Hutton—Yes. Quite often the background is that someone was working here on a two- or four-year visa and fell in love with the place and either went back and came back here ultimately or was able to apply for residency while here and was successful.

Senator HOGG—You say the six months should be extended to 12 months, but even by the evidence that we have heard here today 12 months is really too short a period.

Mr Hutton—It probably should be 12 months as a minimum.

Senator HOGG—It really sounds as if it needs to be in the order of at least two years.

Mr Hutton—Yes. I would not disagree with that.

Senator HOGG—Do you have any actual cases that you can give us which would show graphically the impact if people—

Mr Hutton—I could provide that easily, yes. Are you talking in terms of the issues we touched on earlier affecting their superannuation surcharge levy or Centrelink benefits?

Senator HOGG—Yes. Do that without giving us a large number—just a couple as a sample of the impact—so we can say we are dealing with real cases. Again, we do not want the names and we do not want their private details to be on the public record, but it would certainly help and it would give a little bit of extra weight to the deliberations of the committee, in my view.

Mr Hutton—Certainly. We got a very well documented case early in the piece when it first came to our attention that the surcharge was an issue. He had been issued with this higher rate and was told that the reason for that was the income from the transfer.

Senator HOGG—All right. Do you have one where it impacts on the Centrelink benefits?

Mr Hutton—Yes.

Senator HOGG—If there is one where it impacts on child support—and I do not know how it would—I would be interested to see that as well.

Mr Hutton—I have not had any experience on that one; that was hearsay.

CHAIR—Thank you very much, Mr Hutton. You have brought some new dimensions to the committee, which is always good.

Mr Hutton—Thank you.

[2.51 p.m.]

WHITELEY, Mr Phillip Martin (Private capacity)

CHAIR—Welcome to the hearing. In appearing before this committee you are protected by parliamentary privilege and you have the opportunity to make a request to the committee that all or part of your evidence shall be given in private. We would not expect that to be the case in relation to this particular inquiry. Thank you for taking the time to appear before the committee. We ask you to speak briefly to your submission, which the committee has before it. Do you have any comments to make on the capacity in which you appear?

Mr Whiteley—I appear here as a certified financial planner and I deal on a regular basis with people who have emigrated either recently from the UK or some time ago from the UK. In regard to my submission, I also have some amendments to it, and I have made copies of those amendments.

Senator HOGG—You are from God's own country.

Mr Whiteley—My parents are but I am not. I just spent a lot of time working over there.

Senator HOGG—But you are resident in God's own part of the country.

Mr Whiteley—That is true, I am.

Senator HOGG—It is always good to have an admission like that.

Mr Whiteley—Some of us are lucky.

Senator HOGG—In respect of the examples at page 5 of 7 that you have included for our benefit, do they refer to real people?

Mr Whiteley—Yes.

Senator HOGG—That is great.

Mr Whiteley—I have not brought them with me.

Senator HOGG—If you have said they are real people, I think the committee will accept that they are real people.

Mr Whiteley—In relation to the first one I wrote to the ATO to get them to clarify the situation with surcharge and things. They have now responded generally so if you wanted to see their response I could forward that to you as well.

Senator HOGG—Yes, that would be interesting.

Mr Whiteley—From that you could see the actual numbers tally with exactly what they responded with.

Senator HOGG—Okay. Could you expunge any telling detail to protect the confidentiality and privacy of your clients.

Mr Whiteley—When I wrote to them, I did not specifically put the names in. I gave them all the details of the case but did not give them the names so you can have the whole letter.

Senator HOGG—Fine, that makes it even better. Chair, can I raise an issue? In view of what Mr Whiteley has said to us, it would seem to me that it is important to get a response out of some of the evidence that has come before the committee today from Treasury maybe and/or the ATO?

CHAIR—In respect of certain matters, the secretary will be writing to either Treasury or Tax to confirm certain aspects that the letters raised; but we were not planning to call them back.

Senator HOGG—No. I was not advocating calling them back, but I did think we should at least have their views expressed on the evidence that we have heard today—and maybe views from the likes of Centrelink.

CHAIR—Mr Whiteley, would you care to proceed with your opening statement? There is quite a bit of initial information here that we have to get across.

Mr Whiteley—Certainly. I will not go back over all of my previous submission, because some of that would have already have been covered by previous people and the issues have probably been pretty well explained previously. The main thing I have tried to focus on in the amended submission is to clarify where the people have come from who will actually be impacted by this legislation, so that you can look at what countries they have come from and the volumes of people who are essentially affected by it. I have tried to do that in a couple of different ways. The first is by looking at the actual migration figures going back over the past 25 years—these are all figures obtained from the Department of Immigration and Multicultural and Ethnic Affairs—and I have provided the separate arrivals for skilled migration for the past couple of the years as well. Secondly, on page 3, I looked at arrivals from OECD countries. The reasoning behind that is that most likely the people from these countries would be the ones who had accumulated wealth because they had worked and had accumulated superannuation, and therefore they were the ones likely to be affected by the impact of the legislation in its current form. I did not go back beyond 1975, because most of the people who would have emigrated prior to that had already probably reached retirement and therefore were unlikely to be affected by it, because they were already drawing an income or had left the money in their home country.

You will see from the figures that there have obviously been some changes over the years. The number of migrants coming to Australia from New Zealand has increased quite substantially in the past couple of years. Asia has produced quite a lot of migrants, and more so over periods of political uncertainty; so it is unlikely that those migrants are going to have superannuation, and I have not considered them in the submission at all. Once I established which countries were really affected, I then had a look at what the superannuation arrangements

were in those particular countries and, therefore, at whether they were going to be affected greatly or else not at all. On page 4 I have given a brief outline of the superannuation in the various countries: the United Kingdom, New Zealand, South Africa and basically the Asian region.

The United Kingdom, even in terms of migration numbers, was by far the greatest country for migrant numbers—both for skilled migrants and, over the past 25 years, for normal family migration. The United Kingdom had the most advanced superannuation system, and also one of the more restrictive ones, in that you could not actually cash out your whole benefit. Normally you can only cash out up to a maximum of 25 per cent and the rest must be taken as income. For that reason, we feel that the legislation in its current form is misguided in taxing it as income, because the people actually cannot get access to it and the only way they can bring in the vast majority of it is as a pension scheme when they get to retirement. So adding it to someone's income, and taxing it when they cannot actually get at it because it is locked up until their retirement, seems rather inconsistent. It also makes it very difficult for people to pay the tax. I also think that the changes that, hopefully, will be made to the system will not necessarily disadvantage or make for a more favourable taxation for people who are migrating compared to people who are already resident, since it will be going into superannuation and residents normally would have had their superannuation taxed at a maximum of 15 per cent here anyway. So adjusting the taxation will not, I think, provide an advantage nor a disadvantage, if it is amended.

Those examples, as we heard previously, are actual cases of people that have had benefits. I have also provided one for somebody that is obviously a high rate taxpayer, but only just, who was resident in 1982. He works as a teacher. The vast majority of cases I deal with are, as the previous gentlemen said, teachers, doctors and engineers—professionals but not necessarily high rate taxpayers. I also deal with nurses, who have quite modest incomes, and when they transfer their benefits or when they are assessed they are quite heavily penalised for tax.

Senator HOGG—In example No. 1 you say they have been resident since 1982. When did they transfer the benefit in?

Mr Whiteley—They haven't.

Senator HOGG—They haven't?

Mr Whiteley—No. Because they were coming close to retirement, we looked at it and said, 'How are they going to find $69,000-odd to pay the tax when they cannot cash out any of the benefits?' Even if they take it as a retirement from the UK, it is going to come in as income; if they transfer it to Australia, all they will be doing is paying a high level of tax, waiting until retirement and cashing it out, so there was no real way to meet the bill.

Senator HOGG—Have they been continuously resident in Australia since 1982?

Mr Whiteley—Yes.

Senator HOGG—And their fund in the UK has a large growth factor, of course.

Mr Whiteley—Yes. That is a final salary pension scheme, where the person has left and their pension has been revalued in line with inflation for the last 18 years. Therefore, the difference between the transfer value when they became resident and now, if they transferred it, is where the growth element comes from. So it is not actual physical growth as in equities, it is the increase in the transfer value of final salary scheme—similar to CSS or ComSuper.

Senator HOGG—And the second example?

Mr Whiteley—That is somebody who just has a personal pension. A personal pension would be the something like a—

Senator HOGG—They have not transferred it?

Mr Whiteley—They can transfer.

Senator HOGG—But have they transferred to Australia?

Mr Whiteley—No.

Senator HOGG—For the same reason?

Mr Whiteley—They are really caught, and this is the situation we find with most people: they want to transfer, but they cannot do it because they cannot meet the tax bill. I suppose they are caught between a rock and a hard place. I have shown those two different examples because, if somebody has been resident here for some time—especially in the first example—the retrospective nature of the legislation really hits them. They could not do anything, or there was no reason to transfer before 1994, and then literally overnight they have had all the assessment go right the way back to 1982.

Senator HOGG—When they did not make any contributions, post 1982 anyway.

Mr Whiteley—No.

Senator HOGG—Between 1982 and 1994 they made a nil contribution.

Mr Whiteley—Yes, they would have made nothing. It would have just been their earned entitlement within the company scheme, just being revalued. So they have left, come to Australia and the fund is still sitting in the UK.

CHAIR—An interesting case is in example 1, where the total tax payable, if transferred, is greater than the person's current income of $69,000.

Mr Whiteley—Exactly.

Senator HOGG—We should not laugh.

Mr Whiteley—That is why we all sit there, just scratching our heads. It becomes completely inconsistent and unrealistic.

Senator HOGG—Have you drawn that specific case to the attention of the Australian Taxation Office?

Mr Whiteley—I did not write to them, saying, 'Look, this is XYZ person,' but I wrote to them and said, 'I have this case where someone is earning this much money and this is how much assessed growth they would have within their fund. How would you treat it?' They wrote back and said that they would treat it all as adjusted taxable income for surcharge purposes and that they would treat it all as growth, so I just said, 'You're not going to transfer it.'

Senator HOGG—Game, set and match.

Mr Whiteley—Yes, basically. As you can see, even if you took someone's tax out of their income, they are not going to be on $69,000; they will be on less than that, in their hand. Unless they have the money sitting in a bank account, there is no possible way they could pay it.

CHAIR—With your second example, I would have thought that with your growth component plus your income you would be on 15 per cent surcharge, not 13 per cent.

Mr Whiteley—It worked out at about 101, so on this year's figures, when I worked out the thresholds, it is about 105 on the full surcharge.

CHAIR—At the moment, yes, about 105.

Mr Whiteley—It worked out at 13-odd per cent.

CHAIR—Because of the indexation, is that correct?

Mr Whiteley—That is right. With the second example you can see that the person is nowhere near a higher rate taxpayer and would be nowhere near having surcharge tax to pay. Yet if they transferred their benefit they would pay a substantial amount of tax on the transfer and end up incurring a surcharge on their Australian super. That is why I have used that example in that one.

CHAIR—Thank you. We may well use those in our report.

Senator HOGG—You have answered with some examples the question that I have been trying to have answered all day.

Mr Whiteley—I did this because when I looked through some of the submissions it seemed that everyone was saying, 'It has got to be changed,' but there was no real substance that put it in real life cases. That was the reason for doing it.

Senator HOGG—Congratulations.

Mr Whiteley—I will move on to solutions. Whatever amendments or solutions are made, it would be nice if they fitted in with the existing superannuation system. Obviously there will be a separate wording for overseas transfers, but if any amendments could incorporate or fit alongside the Australian superannuation system that would probably make it a lot easier. If the money, when it is transferred, could go in as an untaxed component, the existing superannuation providers would find it quite easy to deal with that within their own structure because the concept of an untaxed element already exists from government super schemes. A provider could quite easily tax the growth as untaxed and then apply it as post 1983. The balance up until residency could go in as an undeducted, as happens now. That would mean that you are not necessarily identifying different fixed rates of tax specifically for overseas transfers. It makes it quite simple to come straight in as an untaxed.

CHAIR—Even though, on some people's recommendation, you might have paid tax at 15 per cent. Isn't that inconsistent?

Mr Whiteley—It is, but I suppose—

CHAIR—There is a tax liability even though tax has been paid.

Mr Whiteley—It may not necessarily have been paid in the overseas scheme, because some schemes overseas have no tax on them. I suppose it is a case of trying to find some common ground. It is a little inconsistent, but how do you make the system workable for every single possibility? Coming in as untaxed is probably a fair medium and is not taxing it as income. The legislation seems to impact on two different groups of people. One is people who have been here for a length of time. The retrospective nature, and adding it to income, impacts on them more than on people who have recently arrived, simply because the latter will not have had as much growth from their income or on their superannuation. Taxing it as income does not have as big an impact on them as it would on someone who has been here for a long time. Removing the retrospective nature is of more benefit to people who have been here for a substantial amount of time. That will not make any difference to people who are newly arrived, obviously.

Senator HOGG—On an equity basis, how do you argue for removing the retrospectivity now to those who have not transferred their funds as opposed to those who have?

Mr Whiteley—The only way you could do that would be by saying that, if it were changed—and again this would depend on Treasury and whether it was changed—the people who have already moved it and paid the tax would be allowed to go back and have it readjusted to what is the situation now for somebody who has not moved it, to try and keep it equitable. Whether the tax office would want to refund all the tax from somebody I do not know, but you have to ask.

Senator HOGG—That is why I asked the question. You have raised the issue. In effect you are advocating that if the parliament seeks to address the difficulty that people are saying confronts it under 27CAA, our legislation would in its own right have to be retrospective.

Mr Whiteley—Yes. It would be retrospective, but I also think that it would probably fix up the anomaly that has occurred because of the retrospective nature of the original legislation. I do not know how you go about drafting that.

Senator HOGG—Do you have any idea of how many cases would be involved? Are we looking at thousands; are we looking at hundreds? No-one has a database.

Mr Whiteley—No, and that is the problem.

CHAIR—You cannot do that.

Senator HOGG—I know that; that is what I am saying.

Mr Whiteley—And that is part of the difficulty. Even for people who have actually transferred the benefits, there is no real slot to enter it on the tax return. You just have to enter it as other foreign sourced income. So I think the chances of it even being recorded anywhere are pretty unlikely because, on the tax return, it may just come in as other foreign sourced income.

Senator HOGG—What about the concept of tax credits rather than a refund?

Mr Whiteley—I think that would probably work as well to offset against someone's future tax. The only problem I could see is with someone who was getting close to retirement and who did not have a high income. The idea of a tax credit would not necessarily benefit them. That would only benefit somebody who was still paying tax, so that they had something to use it against.

There is one other thing, and I do not know whether it has been covered but I do know that it has been mentioned in a few of the submissions—that is, the foreign investment funds legislation and the fact that it covers only employer sponsored schemes; it does not cover things like personal pensions or, as we would have in this country, master trusts. The FIF legislation is applying and people are meant to be declaring the growth or changing value of their funds, even though they have no way of paying it because it is in a superannuation scheme. So the FIF legislation is discriminating against people who have, say, a personal pension or some sort of private, non-employer sponsored scheme.

CHAIR—That is right.

Mr Whiteley—So I think that changing FIF to allow it to cover all superannuation schemes would make for a more even-handed approach.

Senator HOGG—You have skipped point 4—'extend to 18 months'.

Mr Whiteley—I am sorry.

Senator HOGG—We have heard some say 18 months, and some have said 12 months, and I have heard that even two years might not be sufficient.

Mr Whiteley—I think it might not be sufficient in a limited number of cases. In the majority of cases I have managed to get in within 18 months. There have been a couple that have dragged out over that, and they are more to do with the government regulated schemes in the UK. They seem to be much slower in processing, even if you fax them or try to email them. A

lot of the government schemes do not have email addresses so you have no other option for communication apart from letter.

Senator HOGG—Why wouldn't you err on the side of conservatism and say two years, rather than go down the messy path of saying 18 months and trying to give someone a discretionary power to extend the period beyond that?

Mr Whiteley—The longer the better. I said 18 months simply because I thought that it was a happy compromise between two years and 12 months, and for no other reason. But two years would be good. I think I touched on point 6 when I was talking about allowing people who have already transferred some sort of ability to have the tax credited back to them. That would be nice, but whether it would ever get through is another question. I do not know how willing the tax office is to refund tax already paid, but you have to ask.

Senator HOGG—That is right.

Mr Whiteley—Those changes, especially in treating the transferred amount or the growth as untaxed, would make it easier to collect within the existing superannuation structure for superannuation funds here. If there are future changes in superannuation policy, they would to some extent, hopefully, help protect the situation with English pension transfers or pension transfers from other countries. If it is not a separate item but just all rolled up and part of the existing system, hopefully it will keep pace so you will not then need separate inquiries, committees or meetings to constantly address the overseas issue. Trying to fit it in with the existing superannuation scheme, I think, would save it getting out of step again with superannuation policy generally.

Tax being deducted by the receiving scheme also would then mean that it is out of the self-assessment system. Therefore, the superannuation fund that receives the money here is then responsible for taking the tax out and paying it to the tax office, so it is much more likely that it will get paid and the collection of it will be a lot more seamless. The self-assessment, I think, is a bit hit and miss, because people do not know about the legislation. It is up to the individual to take responsibility for sorting it out. Moving it to the super fund would probably help with compliance.

Moving it to being an untaxed element will remove the issue relating to surcharge, because if it is an untaxed element it is not a contribution; it is not treated as part of income so therefore the surcharge issue goes away. You do not then need separate wordings or legislation specifically to deal with the surcharge. Hopefully, as well, the changes would encourage more people to transfer their benefits. Firstly, they do not have to find the tax to pay themselves. Secondly, it would be more tax effective to get it in here and into our system as soon as possible, simply because the tax effective area is 15 per cent or because franking credits apply. Hopefully, it should also increase tax revenue because of the amount of money that would come in, and that money would then be in our system being taxed as growth. Therefore, in the long run it should increase taxes as opposed to reducing them.

It would hopefully reduce reliance on future state benefits, simply because you have a greater sum of money that will grow for the future and therefore provide for self-funded retirement. It would also increase the amount of investment in Australia. You tend to find that upwards of 55

per cent or more of a fund's assets are invested in the country where it is based. So you find that in Australia a lot of the money goes into cash, property or Australian shares. In the UK it is exactly the same; a lot of the money stays in the UK. You would tend to find that if the money were based here a lot more of it would be invested in Australia, whereas if the money stays overseas in the scheme it would tend to be invested in that country.

Senator HOGG—If the parliament sees fit to legislate to overcome what people have put to us as being inequities, when would be an appropriate time for the legislation to be effected? Obviously, one has to suppose that the parliament will agree, and given the legislative program and the fact that parliament does not like retrospective legislation, for it to be prospective, is there a time that is more preferable in terms of the operation of the legislation?

Mr Whiteley—Do you mean in terms of its actually starting?

Senator HOGG—Yes.

Mr Whiteley—I would say the sooner the better. That has to go through the parliamentary system. Do you mean that if they made it retrospective, from what date?

Senator HOGG—From 1 July. Is that better?

Mr Whiteley—Probably, because it coincides with the tax year. It does not matter too much simply because, with the length of time that it takes sometimes to get the money in, you do not always have control over when the funds eventually arrive. If you start on 1 July, 1 January or some other date, you will not have control over the money coming in. Obviously, I say the sooner the better. I do not think that bringing it during the year would make too much difference. You need to bear in mind that the tax obviously is not shown to the tax office until you submit your tax return. To some extent, if they brought it in, it would then depend on the tax office saying, 'When did the money actually arrive? Did it arrive before the date the legislation started, after or within that year?'

Senator HOGG—Yes, that is what I am trying to find out. Are there any factors that need to be taken into consideration that are not obvious to people like me?

Mr Whiteley—What you would find is that if people knew it was going to start on 1 July they would try to delay the transfer.

Senator HOGG—I am sure they would.

Mr Whiteley—That is just human nature; that is what they would try to do. It would be easier just to say that that is the date it started, be that mid-year or at some point.

CHAIR—Thank you very much. You have brought different aspects to the inquiry, which is very good. It is not easy as the last witness on the last day, so we congratulate you.

Senator HOGG—You have done very well.

Mr Whiteley—No-one has fallen asleep.

CHAIR—Thank you very much. There is another matter that I wish to place on the *Hansard* record. With the agreement of committee members, I wish to read into the *Hansard* record a letter received from a witness who claims to be aggrieved by what the committee considers to be a generic remark made by another witness in relation to any departmental officials appearing before a parliamentary committee. Given that the first witness was not present when those remarks were made I therefore, with the agreement of the committee, will read this letter addressed to the chair of the committee into the record. The letter says:

I refer to my attendance at the Senate committee hearing last Friday (17 May 2002) and the transcript of my comments on page SUPER 9 of the *Hansard* proof available on the Internet. I mentioned to the committee that I had not read Senator Bishop's submission.

While Senator Bishop was giving evidence to the committee I note you specifically sought his comments on this matter (refer page SUPER 17 repeated below}.

I must say that I find Senator Bishop's comments extremely offensive and I am surprised that the committee allowed him to make a comment like that about another witness. I am most concerned that these sorts of comments can be made by a senator, as a witness, about a Treasury officer seeking to be of assistance to the committee and given other workloads such as servicing the needs of Treasury Ministers, especially during Budget week.

I am most disappointed.

Raphael Cicchini, Manager, Superannuation Unit, Treasury.

On behalf of the committee, I also wish to make the following comment. The committee notes Mr Cicchini's concern but was surprised by it. The committee points out that, as a matter of demonstrating professionalism and respect for a parliamentary committee, it is the committee's expectation that Treasury officials would have read the submissions in preparation for a public hearing. This is particularly so because Treasury is the body with the responsibility and knowledge of the policy issues surrounding the inquiry and is the best placed department to advise the committee on the matters raised in the submission. That concludes the committee's proceedings. On behalf of the committee, I thank all witnesses who have given evidence today.

Committee adjourned at 3.25 p.m.