

D. G. & M. H. LETHBRIDGE

The Secretary of the Committee
Joint Standing Committee on Public Accounts and Audit
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16 March 2006

Dear Madam/Sir,

Submission to the “Inquiry reviewing a range of taxation issues within Australia”

This submission concerns the first term of reference, namely the impact of the interaction between self-assessment and complex legislation and rulings. It identifies a particular problem where the ATO will not issue a ruling, and utilises my experience with the ATO as an illustration.

In my capacity as a trustee of a Self Managed Super Fund (SMSF) I recently attempted to obtain certainty in an area of complex legislation by way of a definitive ruling from the ATO. Very substantial penalties can be invoked if the trustee is subsequently found to have made the wrong decision in this area.

The question was relatively simple, namely whether a particular Member has a “grandfathered” defined benefit pension entitlement.

The facts in brief are as follows. It was reported to a SMSF meeting that the Member had applied for a defined benefit pension. An actuarial review had been obtained and it was agreed and minuted on 29 June 2003 that the pension would be paid as early as possible, either on the Member’s retirement or earlier if the relevant legislation should so allow. The pension was approved and became part of the Governing Rules of the Fund, but the Member continued working and could not commence the pension.

From 12 May 2004 legislation effectively banned (subject to transitional rules) all new such pensions from commencing in SMSFs, unless the entitlement to the pension was established before 12May2004.

The ATO would not make a binding decision on this matter (despite two attempts). The ATO stated in their reply dated 9 November 2005 that “a private ruling could not be given as they are only available on income tax matters involving extent of liability”. In place of a ruling they provided attachments and the following written advice:

*An SMSF can continue to pay a defined benefit pension where
The term of the pension commenced or
The entitlement to the pension was established,*

before 12 May 2004, even if the payment is not made until on or after 12 May 2004. These are sometimes referred to as “grandfathered pensions”.

This advice was consistent with that already obtained in 2004 from the relevant Minister’s office and indicated the pension could be paid, but this advice is not legally binding on the ATO. Because an incorrect interpretation can apparently lead to a truly Draconian outcome, namely the potential confiscation of almost half the Member’s superannuation assets, the trustee sought greater certainty.

As it appeared in discussion with the ATO that the first request for a ruling might have emphasised the SIS regulations at the expense of the Tax Acts, a second application (with similar attachments) for a private binding ruling was made on 27 January 2006.

The first request was:

Can I as a trustee of a self managed superannuation fund (SMSF), pay a new defined benefit pension to a member under Division 9.2B of the Superannuation industry (Supervision) regulations 1994 (SIS Regulations)?

The revised request was:

What is the extent of the liability to the ATO of the XXX self managed superannuation fund (SMSF) when it commences to pay a new defined benefit pension on 1 July 2006 (when the member retires) in accordance with a resolution of the SMSF made on 29 June 2003 (when the terms and conditions of the pension were established)?

The reply dated 10 March 2006 was in general terms only and did not take any account of the specific issue of the pre 12 May 2004 pension entitlement.

In subsequent phone discussions the ATO stated that private binding rulings could not be made for SMSFs, because SMSFs were not in the Tax Acts. The ATO person said that if the trustee felt uncertain about the pension, the trustee could gain comfort because the fund could show the ATO correspondence to date, should there be any queries about the validity of the pension in the future. I was told that with regard to penalties the ATO would look favourably on all the various attempts already made to achieve some measure of certainty.

The trustee believes it is unfair that the body charged with interpreting and implementing the SMSF laws and then levying penalties, should place the onus of prior interpretation back on the trustee, given the extreme severity of the penalties involved.

Why cannot the ATO make private binding rulings with regard to SMSFs?

David Lethbridge