

The Senate

Economics Legislation Committee

Provisions of the Taxation Laws Amendment
(Superannuation Contributions Splitting)
Bill 2003 and associated regulations

December 2003

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Chapter 1

INTRODUCTION

Introduction and referral

1.1 The Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003 was passed by the House of Representatives on 17 September 2003. On the same day it was referred to the Senate Economics Legislation Committee for consideration and report by 3 November 2003.

1.2 On 13 October 2003 the Department of the Treasury issued a series of draft regulations to give effect to the proposed changes to superannuation splitting arrangements foreshadowed in the bill. These regulations were: the Superannuation Industry (Supervision) Amendment Regulations (draft), the Income Tax Amendment Regulations 2003 (draft) and the Retirement Savings Accounts Amendment Regulations 2003 (draft).

1.3 On 27 October 2003, on a motion by Senator Sherry, the Senate agreed to extend the Committee's terms of reference to include consideration of these draft regulations concurrently with the Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003. At the same time the Committee's reporting date was extended to 3 December 2003.

Purpose of the bill and regulations

1.4 The Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003 does not of itself provide the legislative basis for the splitting of superannuation contributions. Rather, it deals with consequential amendments related to proposed changes to the *Superannuation Industry (Supervision) Act 1993*. It also amends the *Income Tax Assessment Act 1936*, to ensure that appropriate taxation status is given to a split contribution when it is rolled over to another account or fund, and the *Superannuation Contributions Tax (Assessment and Collection) Act 1997*, to ensure that any surcharge liability attached to the original contribution is unaffected by the split.

1.5 Although the Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003 does not provide the legislative basis for contributions splitting, the Explanatory Memorandum issued with the bill sets out the rationale for the policy change, as follows:

The splitting of superannuation contributions will assist families to maximise the benefits available in superannuation and provide an avenue for spouses to share in superannuation benefits. It will be of particular benefit to low income or non-working spouses by allowing them to have superannuation assets under their own control and have their own income in retirement.

It will provide single income couples, including those not able to make voluntary contributions, with access to two ETP low-rate thresholds and two reasonable benefit limits in the same way as dual income families.¹

1.6 The Explanatory Memorandum also sets out the Government's intention to split superannuation contributions annually. The details of this approach are set out in the regulations. The background to the adoption of this approach is described in chapter 2.

Submissions

1.7 The Committee advertised its inquiry into the Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003 on the internet and in *The Australian* newspaper. In addition the Committee contacted a number of organisations alerting them to the inquiry and inviting them to make a submission. A list of submissions received appears at **Appendix 1**.

Hearings and evidence

1.8 The Committee held one public hearing at Parliament House, Canberra, on Tuesday 25 November 2003. Witnesses who appeared before the Committee at that hearing are listed in **Appendix 2**.

1.9 Copies of the Hansard transcript are tabled for the information of the Senate. They are also available through the internet at <http://aph.gov.au/hansard>.

Acknowledgment

1.10 The Committee wishes to thank all those who assisted with its inquiry.

1 Explanatory Memorandum, Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003, p. 3.

Chapter 2

THE BILL AND REGULATIONS

Introduction

2.1 This chapter describes the background to the proposed legislative changes, outlines the main provisions of the bill and regulations and their expected financial impact and explains the rationale for the Government's decision to opt for an annual contributions splitting model in preference to the three other models described in the Explanatory Memorandum.

The background

2.2 At the last election the Government gave a commitment to legislate to allow members of superannuation funds to split both their personal and their employer superannuation contributions with their spouse. The Government had previously legislated (in 1997) to allow members of superannuation funds to make voluntary superannuation contributions to their spouse but the existing arrangement does not cover employer contributions. The exact mechanism by which personal and employer superannuation contributions were to be transferred to a spouse was not finalised at the time of the election.

2.3 To give effect to the election commitment, and to canvass opinions on possible mechanisms for doing so, the Government released a Consultation Paper in July 2002 outlining three possible options. These were, briefly:

- **Prospective splitting (option 1)**

After a member notifies his/her superannuation provider of an intention to split, each subsequent contribution would be split.

- **Annual splitting (option 2)**

A member notifies his/her superannuation provider annually of an intention to split contributions received during the previous year. The contribution would then be split annually and retrospectively.

- **Joint accounts (option 3)**

A member wishing to split superannuation contributions would open a new account, with their existing superannuation provider, to be held jointly in their own and their spouse's names. At the request of the splitting spouse the superannuation provider would deposit all or part of the splitting spouse's contribution into this account.

2.4 During consultations on these options most of the individuals and organisations consulted opposed option 3 because it would require fundamental changes to the superannuation system and be costly to participants, who might be required to maintain three accounts. They generally preferred option 2 to option 1

because of its lower cost and reduced administrative complexity. However, the majority favoured a fourth option, not included in the Consultation Paper, which was to split benefits rather than contributions and to do so at the time of retirement (for reasons discussed in the following chapter.) In recognition of the level of support for this option it was included in the Government's Regulation Impact Statement accompanying the Explanatory Memorandum.¹

Main provisions of the bill and regulations

The bill

2.5 The main provisions of the bill are intended to amend the *Income Tax Assessment Act 1936* and the *Superannuation Contributions (Assessment and Collection) Act 1997* to provide for the tax consequences of superannuation splitting. As noted in chapter 1, the basic principles of the taxation treatment of contributions splitting are set out in the Explanatory Memorandum as follows:

The splitting of superannuation contributions will assist families to maximise the benefits available in superannuation and provide an avenue for spouses to share in superannuation benefits. It will be of particular benefit to low income or non-working spouses by allowing them to have superannuation assets under their own control and have their own income in retirement.

It will provide single income couples, including those not able to make voluntary contributions, with access to two ETP low-rate thresholds and two reasonable benefit limits in the same way as dual income families.²

2.6 The way in which the superannuation splitting mechanism will operate is specified in the regulations.

The regulations

The Superannuation Industry (Supervision) Amendment Regulations 2003

2.7 These regulations set out the way in which superannuation splitting is to operate—that is, annually for the previous financial year. It also defines a deductible contribution and an undeducted contribution and specifies the maximum percentage of each component which can be transferred from the sending spouse to the receiving spouse.

1 Explanatory Memorandum, Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003, pp. 24-26.

2 Explanatory Memorandum, Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003, p. 3.

The Income Tax Amendment Regulations 2003

2.8 These regulations provide that the money transferred from a sending spouse to a receiving spouse is to be considered a ‘contributory splitting eligible termination payment’ for taxation purposes, in line with the requirements of the *Income Tax Assessment Act 1936*. They also set out the manner in which a superannuation fund is required to advise the Australian Tax Office of the details of the fund to which a split contribution has been made.

Retirement Savings Accounts (RSA) Amendment Regulations 2003

2.9 These regulations set out the way in which superannuation splits are to operate in cases in which money is transferred to an RSA rather than to another superannuation fund, or another account in the same superannuation fund. It parallels the regulations set out in the Superannuation Industry (Supervision) Amendment Regulations.

Financial implications of the bill and regulations

2.10 In the Explanatory Memorandum the Government has costed³ three of the options discussed. The fourth option (splitting of benefits at the time of retirement) is not costed but is estimated by the Government to be significantly greater in the longer term than the other three options.

2.11 The Government’s preferred approach – option 2 – is estimated to cost \$6 million over the three years from commencement. This is significantly less than the \$11 million allocated in the 2003-2004 Federal Budget. The discrepancy can be explained by the fact that in option 2 contributions are split at the end of the financial year, which defers costs by one year.

The rationale for choosing annual contributions splitting (option 2)

2.12 The advantages and disadvantages of each of the options are discussed in the Explanatory Memorandum.⁴ Options 1 and 2 are said to meet the Government’s objective of providing tax advantages and other benefits to couples where one is out of work or has a significantly lower income than the other. These advantages are summarised as follows:

- Access to two ETP low-rate thresholds and two reasonable benefit limits;
- Providing the low income or non-working spouse with their own superannuation assets under their own control...and their own income in retirement; and

3 These are costs to government. Costs to superannuation funds and individuals are not estimated in the Explanatory Memorandum

4 Explanatory Memorandum, Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003, pp.17-27.

- For members of some superannuation funds, splitting may provide the low income or non-working spouse with improved access to cost-effective death and disability insurance.⁵

2.13 Options 3 and 4 provide similar benefits (although control by the non-working spouse is limited to retirement income rather than superannuation). In addition, the Government claims that option 4 will not provide non-working spouses with improved access to cost-effective death and disability cover. This claim is disputed in evidence to the Committee where it was suggested that none of the options will do this (as discussed in the following chapter).

2.14 The deciding factor in choosing option 2 is, according to the Explanatory Memorandum, its lower cost to superannuation funds.

Option 2 is expected to impose smaller costs on superannuation providers than option 1, and therefore is the preferred option.⁶

2.15 However, option 2 also entails the lowest cost to government (\$6 million as opposed to \$11 million for options 1 and 3 and uncosted but significantly higher estimates for option 4). Some submissions claimed that this was also a factor in the decision to adopt option 2.⁷ Furthermore, most of the evidence to the Committee suggested that, while option 2 imposed fewer costs on superannuation funds than option 1, option 4 would impose the lowest costs of all the options both for funds and for contributors.

2.16 A number of the witnesses at the public hearing pointed to the difficulty of assessing the relative costs of each of the options and the inadequate information provided by government to assist them in doing so.

2.17 These issues are discussed in greater detail in the next chapter.

5 Explanatory Memorandum, Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003, p. 20.

6 Explanatory Memorandum, Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003, p. 27.

7 See for example, Institute of Chartered Accountants, Submission 4, p. 3 and Investment & Financial Services Association Ltd, Submission 11, p. 3.

Chapter 3

EVIDENCE TO THE INQUIRY

Introduction

3.1 All inquiry participants supported the Government's intentions in framing the legislation. The following comments are typical of those received on this issue.

We are very supportive of the concept of enabling spouses to split their superannuation. Many couples need to make choices about whether one or both parties become or remain gainfully employed. Often one party needs to sacrifice their own career in order to care for children or other family members. It is therefore reasonable to treat a couple's retirement savings as a joint investment rather than the current system where only the working spouse is entitled to superannuation.¹

The FPA welcomes the splitting of super contribution initiative, as an important planning matter in securing families' financial future.²

3.2 However, most inquiry participants expressed concern with the Government's choice of option 2. These concerns are discussed below, beginning with those most frequently articulated in the evidence.

Concerns with option 2

Costs and administrative complexity

3.3 The major concerns related to the costs, both to superannuation funds and to members, and to the administrative complexity of the proposal.

The option adopted for the implementation of this legislation will result in an increase in fund administration costs in particular for those members opting to split their contributions...

Overall this will result in a lower superannuation pool as households will bear the increased administration costs associated with having two superannuation accounts and the annual costs of splitting contributions.³

3.4 The costs to the funds will, it was claimed, be passed on to fund members, including those unable to benefit from this measure. It would thus be highly inequitable in its impact.

1 Mercer Human Resources Consulting Pty Ltd, Submission 2, p. 1

2 Financial Planning Association of Australia Limited, Submission 16, p. 1

3 The Institute of Chartered Accountants in Australia, Submission 4, p. 2.

It is not at all clear from the legislation the extent to which any of these costs can be recovered, if at all, from the spouses who take advantage of this measure. Even if funds were able to charge on a 'user-pays' basis, any amount levied is unlikely to begin to recoup the amount of any costs incurred. Accordingly, cross-subsidisation by members who are ineligible to benefit from this measure raises considerable questions of equity.⁴

3.5 The costs to members were quantified in a number of submissions and at the public hearing.

The administration work required to transfer split contributions would be comparable to that required for any other benefit payment (eligible termination payment). As an indicative amount, we note that our current superannuation fund clients charge their members an average annual administration fee of \$52 and an average benefit payment fee around \$70. The benefit payment fee alone is equivalent to over 3% of an equal split of annual employer contributions for a full-time employee on average earnings.⁵ Payment fees imposed for Family Law splits by our current superannuation fund clients range from nil to \$100.⁶

3.6 The cost to funds over a three year period was estimated by one submission⁷ at more than \$70 million. Figures provided at the public hearing suggested a start up cost of \$8 million and annual running costs of \$800,000.⁸

3.7 The administrative complexity of option 2 was described in one submission as follows:

The 'annual [contribution] split' model will have significant implications for the administration of superannuation funds and will necessitate incurring considerable costs in amending information technology systems and infrastructure, altering processes and procedures, changing documentation and in training and supervising staff.⁹

4 Superpartners Pty Ltd, Submission 12, p. 3.

5 Calculated as a transfer of 50% of employer contributions (9% of full time adult average weekly ordinary time earnings quoted in ABS figures for February 2003): 50% x 9% x \$48,896 = \$2,200

6 Australian Administrative Services, Submission 14, p. 4. For other cost estimates see also: Mercer Human Resource Consulting, Submission 2, p.2, and Institute of Actuaries, Submission 5, p. 2. See also *Transcript of Evidence*, Davison M. p. E8 and Maroney J, p. E15

7 Association of Superannuation Funds of Australia, Submission 6, p. 7.

8 *Transcript of Evidence*, Brady H. and Stanhope W. p. E 32

9 Superpartners Pty Ltd, Submission 12, p. 3. See also Association of Superannuation Funds of Australia Ltd, Submission 6, p. 4, which lists the administrative changes required to set up an annual contributions splitting regime.

Underutilisation

3.8 Inquiry participants considered option 2 was likely to have a low take up rate because its complexity makes it difficult for people to understand its potential benefits. Because those most likely to benefit were least likely to have access to the financial advice necessary to make an appropriate decision in their particular circumstances, the measure will also serve to exacerbate existing inequities in superannuation coverage.

We expect that contribution splitting may be under utilised, particularly by lower and middle income workers due to the approach being proposed by Government.¹⁰

This measure assumes members understand the end benefit taxation rules as well as having the skills to compare the costs of splitting with the tax benefit available. Those couples that find this too hard may choose to either split contributions just in case or not split at all. Each situation could result in a negative outcome.

...this means that the measure is likely to advantage those with the resources to obtain advice on the benefits of the strategy and to make informed decisions and lead to inequities amongst like participants in the community.¹¹

Cbus is concerned that this model will only benefit those couples who are knowledgeable about superannuation. The bill will create increased demands for financial advice which will represent another cost to superannuation members. Those couples that are not aware of the legislative changes and who do not arrange their financial affairs to their advantage will suffer reduced retirement incomes compared with those that do.¹²

3.9 In addition, it was claimed, only a relatively small group of people is in a position to benefit from option 2.

It is difficult to see how the ability to split contributions may encourage new or increased contributions into the fund. Spouse contributions have been available since 1997- if the couple had the capacity to make new or increased contributions they can make spouse contributions. Splitting of the benefit [sic] is really only of use either for low-income couples who can only afford to split employer contributions or high income couples who are able to take advantage of the two tax free thresholds and reasonable benefit limits.¹³

10 Mercer Human Resource Consulting, Submission 2, p. 3.

11 The Institute of Chartered Accountants in Australia, Submission 4, p. 2

12 Cbus, Submission 9, pp. 1-2.

13 Superpartners Pty Ltd, Submission 12, p. 5.

Contribution splitting limited to accumulation funds

3.10 Option 2 excludes members of defined benefit funds from contribution splitting arrangements, even if they have an accumulation component in that fund.

The Explanatory Memorandum (confirmed by draft Regulation 6.40) indicates that contribution splitting will only be available to members of accumulation funds.

..Many members of defined benefit funds have both accumulation and defined components of their benefits. It would be desirable for the same splitting rules to apply to all members.¹⁴

For members entitled to defined benefits, the complexities are such that splitting contributions is not viable. On the other hand, the alternative approach of benefit splitting could be applied equally to defined benefit and accumulation members.¹⁵

Discriminatory

3.11 A number of submissions argued that option 2 is discriminatory when compared with the position of divorcing couples who are able to split their superannuation benefits at the time of separation.

Divorcing or separating couples are already able to split their superannuation benefit. If married couples are only able to split contributions and not benefits, this would discriminate against those couples who remain married in favour of those who separate. We believe that those who remain married should not be discriminated against in this manner.¹⁶

Option 2 will not achieve the Government's objectives

3.12 A number of participants claimed that the legislation, as currently drafted, will not achieve the Government's objectives as set out in the Consultation Paper and the Explanatory Memorandum.

While ASFA acknowledges the need to contain revenue impacts for government by limiting the quantum of an account balance that could be split on retirement, it strongly argues that the splitting option currently favoured by the government will not, for most people, deliver the benefits anticipated by the Consultation Paper.¹⁷

14 Australian Administration Services, Submission 14, p. 5

15 Mercer Human Resource Consulting, Submission 2, p. 3.

16 Mercer Human Resource Consulting, Submission 2, p. 4.

17 Association of Superannuation Funds of Australia Ltd, Submission 6, p. 13.

We do not believe that the Bill will fulfil the policy intent in the most efficient or equitable manner.¹⁸

Lack of clarity in the legislation, as drafted

3.13 It was suggested in a number of submissions that lack of clarity in the drafting of the regulations may result in unintended consequences and further hamper the fulfilment of government objectives in this legislation.

3.14 A particular concern was raised in connection with the provisions relating to the funds required to be held in the accounts of splitting members. As drafted, the Superannuation Industry (Supervision) Amendment Regulation (SISAR) allows no discretion for a trustee to adjust the contribution split application form. While SISAR limits the contributions split to 70% of deducted contributions, to allow for contribution tax and the superannuation surcharge, it overlooks the fact that deductions from the fund can exceed the amount remaining in the fund, requiring the fund and its members to make up the shortfall.

The amount of the split is limited to 70% of deductible contributions to allow for contribution tax and the superannuation surcharge.

Despite this, it would still be possible (for example, as a result of insurance premiums, administration fees, and/or negative investment returns) for a member's balance at the time of a split to be less than the sum of the contributions received during the previous year. In such a circumstance, the draft regulations would still require a benefit payment in line with the member's instructions. This would result in a requirement for a fund to subsidise one member's contribution splitting from the accounts of other members of the fund.¹⁹

Our most significant concerns relate to:

The requirement for the trustee to transfer amounts to the receiving spouse's fund even though

- in some circumstances, the available benefit of the sending spouse will be insufficient to meet the payment
- the sending spouse's fund will continue to be liable for surcharge assessments even though the benefit remaining is insufficient to meet the payment.²⁰

3.15 Other areas in which the legislation, especially the regulations, is unclear and/or may have unintended consequences were said to relate to:

18 Australian Administrative Services, Submission 14, p. 1.

19 Australian Administration Services, Submission 14a, pp. 2-3. This issue is described in some detail in Institute of Actuaries of Australia, Submission 5a, pp. 4-5.

20 Mercer Human Resource Consulting, Submission 2a, p. 1.

- The position of a defined benefit member who leaves the service and retains a benefit in the fund as an accumulation interest;²¹
- Failure to achieve the Government's intention to prevent a fund becoming a public offer fund;²²
- Regulations relating to conditions of release are unworkable;²³
- Lack of clarity on the percentage of deductible and undeducted contributions that can be split;²⁴
- Regulations relating to the timing of an application for splitting are unnecessarily constrained and could be liberalised without affecting the Government's intended timing for transfer;²⁵
- FSR and disclosure implications of establishing an account for the receiving spouse not covered in existing regulations;²⁶
- Regulations require insufficient information to be provided by applicant in respect of receiving spouse;²⁷
- Regulations do not reflect the fees associated with processing any application and rollover or transfer;²⁸ and
- The regulations do not adequately cover the position of self employed people.²⁹

Other concerns

3.16 Other concerns with option 2, raised in a small number of submissions, relate to:

- The failure to include same sex relationships;
- The discriminatory nature of the specified conditions of release;
- Member protection provisions for the receiving spouse;
- Potential for fraud in annual splitting arrangements;
- Interrelationship with social security system; and
- Provides disproportionate benefit to higher income families.

21 Submission 5a, p.6.

22 Submission 5a, p.6.

23 Submission 5a, p. 6, Submission 14a, p. 4 and Submission 2, p.7.

24 Submission 5a, p. 7, Submission 14a, p.2 and Submission 2a, pp.2-3.

25 Submission 5a, p. 8, Submission 12, p. 15 and Submission 14a, p. 4.

26 Submission 6, p. 11 and Submission 14a, p. 4.

27 Submission 6, p. 12.

28 Submission 6, p. 12.

29 Submission 8, p. 4. Submission 12, pp. 12-18 and Submission 2a, pp. 3-13 provide a detailed critique of the legislation.

Support for option 2

3.17 Two submissions to the Committee did not express a preference between options 1 and 2³⁰ and two supported option 2.³¹

3.18 The Corporate Superannuation Association explained its support for option 2 as follows:

The Corporate Superannuation Association supports the model that is presented in this legislation. Annual splitting is fine by us. Senators would be aware that, in the typical corporate fund, member fees are lower than in other models and Corporate, with admittedly fewer members and with bigger balances, feel that annual split, from our point of view, is quite satisfactory.

...We are, however, concerned about administrative burdens in reporting these matters.³²

3.19 The Women's Action Alliance (WAA) set out its reasons for supporting option 2 in its submission. While many of the reasons given in this submission for supporting option 2 apply also to option 4, the WAA favours option 2 for the following reasons:

- It allows low and middle income earners to keep their superannuation accounts alive and growing during periods of absence from the work force;
- It ensures that the impact of compounding interest on superannuation assets continues to operate during periods of absence from the work force;
- By providing women with a continuously active superannuation account this option will play a valuable role in educating them about superannuation;
- It provides women in the unpaid work force with death and disability cover;
- It enhances the status of unpaid work;
- It gives the single income family the ability to eliminate taxation disadvantages by providing two tax free thresholds; and
- It ensures some provision for the wife in the event of a subsequent marriage breakdown.

3.20 The Women's Action Alliance submission therefore concluded:

The degree to which women are disadvantaged in the accumulation of superannuation assets due to their reduced and broken participation in paid work is well documented. The need to address this has been widely

30 Australian Industry Group, Submission 3 and Sunsuper Pty Ltd, Submission 13.

31 Corporate Superannuation Association Inc, Submission 15 and Women's Action Alliance, Submission 10

32 *Transcript of Evidence*, Cerche M. p. E24.

recognised for several years and we heartily welcome the Government's initiative in this direction....We therefore believe the reform that this legislation enables is essential to offer women the opportunity to achieve greater security and independence in retirement.³³

3.21 At the public hearing WAA representatives stated that, while they much preferred option 2 to all of the options under discussion, they would be prepared to support option 4 if it could be demonstrated that this was a better way of securing access to superannuation and retirement income for women outside the paid workforce.

Our preferred model is still splitting throughout the marriage, particularly during those periods when the woman is not in paid work. However if, in the wash-up, it does prove to be to the couple's greater economic advantage to only split on retirement, at draw-down time, then we are certainly interested in that option too and we are open to it as long as all couples will be eligible for that.³⁴

Support for benefit splitting (option 4)

3.22 Most contributors to the inquiry favoured option 4. Their reasons for doing so are discussed below, with the most frequently cited reasons discussed first.

Lower cost and less administrative complexity

3.23 Option 4 is the least complex of all the options from an administrative point of view. It involves only one set of transactions – at the time of retirement – rather than annual transfers as in option 2. As each transfer is costly for the funds, and consequently for members, option 4 is also the cheapest of the options, for the funds and for members. By reducing costs to members, it maximises their benefits.

Insofar as the superannuation funds are concerned, effecting the split at the time the superannuation benefit is to be paid to the member would be significantly easier than the 'annual split' model.

Most obviously, the impact would only occur at one point in the member's thirty to forty year membership and would only require some relatively minor amendments to the benefit payment procedure at the point the member takes their benefit.³⁵

Administration costs are a significant issue with the contribution split as envisaged in the Bill

...Administration costs are significantly lower on benefit splits – for example, one company suggested that to split a rollover would add only

33 Women's Action Alliance, Submission 10, p. 1.

34 *Transcript of Evidence*, Smit P. p. E19.

35 Superpartners Pty Ltd, Submission 12, p. 4.

marginal cost to the process. Most importantly, a benefit split would occur once, rather than every year, and then only if the benefits outweigh the costs.³⁶

Higher take up rate

3.24 It was suggested that option 4, being less complex than the other options, would be likely to attract support from more lower and middle income earners than would the other options. Furthermore, it would come into operation at the time of retirement, which is the only time, it was suggested, that many people seek financial advice. They would thus not suffer the disadvantage inherent in option 2, the benefits of which might not be apparent to people who did not seek financial advice. A higher take up rate would help fulfil the Government's objective of extending and enhancing superannuation opportunities for those individuals least likely to enjoy them.

With respect to the couple, the most expedient time for them to share their superannuation benefits is at the time the benefit is to be paid to the member. It is at this time that the couple is best placed to evaluate the most effective split of the benefit to maximise income in retirement and to access the two ETP low-rate thresholds and Reasonable Benefit Limits.³⁷

Low and middle income earners would be more likely to utilise the [benefit splitting] system creating an eventually greater retirement entitlement for non-working or low income spouses.³⁸

Consistency with treatment of superannuation under Family Law

3.25 The Family Court regards accumulated superannuation funds as joint assets. Recent Federal legislation provides for superannuation assets to be split after divorce. Adoption of option 4 would provide the same rights to couples who remain married.

An analysis of the administration process required for a **benefit split** system which has recently been undertaken reveals striking similarities with the administration processes funds have developed to implement the Family Law changes. Splitting end benefits would allow funds to build on and take advantage of the work already done in implementing the Family Law changes and would significantly reduce both implementation and total transaction costs.³⁹

Divorcing or separating couples are already able to split their superannuation benefit. If married couples are only able to split contributions and not benefits, this would discriminate against those couples

36 Investment & Financial Services Association Ltd, Submission 11, p. 2.

37 Superpartners Pty Ltd, Submission 12, p. 3.

38 Mercer Human Resource Consulting, Submission 2, p. 1.

39 Association of Superannuation Funds of Australia Ltd, Submission 6, pp. 12-13.

who remain married in favour of those who separate. We believe that those who remain married should not be discriminated against in this manner.⁴⁰

Option 4 can include defined benefit funds

3.26 Unlike option 2, which is restricted to accumulation funds, option 4 can include defined benefit funds. This is particularly valuable for defined benefit members who are also entitled to accumulation benefits.

[in option 4] There is the potential to extend the benefit to members with a defined benefit interest. This could be achieved by adopting valuation principles similar to those to be used when valuing an interest for the purposes of family law agreements.⁴¹

Case against option 4

3.27 In its Explanatory Memorandum the Government provides three main reasons for preferring option 2 to option 4. Each of these is discussed below, together with the contrary views expressed by inquiry participants.

Option 4 will not provide access to death and disability insurance for a non working spouse

3.28 Inquiry participants did not dispute this. However, they questioned whether **any** of the options would do so. Suggesting that they would not, participants concluded that this was not a reason for supporting option 2 over option 4.

We note that, in most cases, superannuation funds are unable to find insurance cover for disability benefits for those not in the workforce. Even death cover may not always be available and generally requires greater levels of health evidence and higher premiums than that offered to employees. The use of this argument in justifying contribution splitting is therefore tenuous.⁴²

Option 4 does not provide the non working spouse with control over their superannuation

3.29 While inquiry participants did not generally dispute this, they considered the argument was irrelevant. They suggested that, where a working spouse was reluctant to contribute to a non-working spouse under existing arrangements they would be unlikely to do so under option 2 and so the non-working spouse would obtain no benefits during the accumulation phase in either option 2 or option 4. If a working spouse was willing to contribute, then current arrangements allow this (for personal contributions).

40 Mercer Human Resource Consulting, Submission 2, p. 4.

41 Association of Superannuation Funds of Australia, Submission 6, p. 10.

42 Mercer Resource Consulting, Submission 2, p. 6.

The superannuation system currently allows for some splitting through the availability of spouse contributions. Members which are not supportive of relinquishing control of additional savings are unlikely to relinquish control of employer contributions. This will not necessarily benefit those persons in relationships where one party is in financial control of the household assets.⁴³

The ‘control’ argument is not directly relevant to a voluntary scheme. Couples who are likely to share superannuation via a voluntary splitting mechanism would also be likely to share decision-making about family assets, including superannuation in the name of only one spouse. If spouses do not currently share control over matrimonial assets, it seems highly unlikely they would use a voluntary scheme to split superannuation. If the couple separates, the Family court is able to order a fair split of superannuation (as with other matrimonial assets). Otherwise, Government rarely intrudes into the ordinary decision-making of couples – to use this argument in superannuation sits at odds with the usual distinction between private and public issues.⁴⁴

3.30 Some participants asserted that separate control was not necessary.

We accept that benefit splitting does not immediately enable non-working spouses control over superannuation assets to the same extent as contribution splitting. However, we do not see this as a significant flaw. With divorcing and separating couples able to split superannuation, the need for control during the accumulation phase is not as relevant as it may otherwise have been because each spouse will have a right to share in the couple’s overall superannuation assets.

A benefit splitting approach would still enable spouses to control their own share of the couple’s superannuation savings in the retirement phase.⁴⁵

3.31 Others thought the additional costs to the non-working spouse of option 2 outweighed the benefits of control

This option [option 4] does not immediately enable the non-working spouse to have control over superannuation assets to the same extent as contribution splitting, but it achieves the other objectives to a greater degree and ultimately gives the non-working spouse a larger retirement amount and greater flexibility and control of savings in the retirement phase.⁴⁶

43 Institute of Chartered Accountants in Australia, Submission 4, p. 2.

44 Investment & Financial Services Association Ltd, Submission 11, p. 2. See also *Transcript of Evidence*, Stanhope W. p. E29, which describes the ‘control’ argument as a furphy.

45 Mercer Human Resource Consulting, Submission 2, p. 5.

46 Association of Superannuation Funds of Australia Ltd, Submission 6, pp. 5-6.

Option 4 is more costly to government

3.32 Some submissions disputed the assertion that option 4 is more costly to government, arguing that the additional costs to revenue from this measure would be offset by lower deductions to funds for administrative costs (in comparison with the costs incurred in implementing option 2).

ASFA [Association of Superannuation Funds of Australia Ltd] considers that splitting at the benefit stage would be revenue neutral for a not insignificant number of years as the revenue costs of any additional splitting would be more than offset by lower tax deductions for administrative costs by funds.⁴⁷

3.33 Some participants suggested that option 4 would be more costly to government only because more people could be expected to take it up.

The key argument for opposing the benefit method of splitting contributions is the increased cost to government although it was acknowledged that this was identified as the most efficient model for the remainder of the participants. The increased cost to government can be attributed to the increased take up of the measure highlighting the inherent inequity in the method of implementation chosen.⁴⁸

It is our view that the lower cost to Government revenue associated with contribution splitting will primarily be as a result of lack of use due to high administrative cost, lack of understanding and general inertia.⁴⁹

3.34 Option 4 was not costed in the Explanatory Memorandum and the basis for the costing of the other options was not explained. Nor did the Explanatory Memorandum give any indication of likely take up rates of each of the options. In this circumstance it was difficult for witnesses to assess the accuracy of government estimates of the cost of each of the options and to suggest means by which costs to government might be contained.

We had a major option – the one that the industry has proposed [option 4] – which we would think solves all of the policy objectives, which was not on the table. It was not on the table for a variety of reasons, including containment of fiscal costs. We have attempted to look at the ways to contain fiscal cost, because we certainly think there are means to do that relatively simply. ASFA discussed some in their evidence, we have discussed some in our submission. There are a couple of ways of approaching it depending on how you want to do it. But in the absence of an

47 Association of Superannuation Funds of Australia Ltd, Submission 6, pp. 8-9.

48 Institute of Chartered Accountants in Australia, Submission 4, p. 3.

49 Mercer Human Resource Consulting, Submission 2, p. 5.

open debate about costs it has been very hard for us to make any traction on those sorts of issues.⁵⁰

3.35 Treasury representatives at the public hearing were unable to provide any details of the basis on which the costings had been made or on the costs to superannuation funds of the various options. They agreed that Treasury had undertaken some work on this and had concluded that option 4 would be more costly than its preferred option and that it would not fulfil the policy objective of providing spouses outside the paid work force with control of their superannuation before retirement.

...Generally, the government has considered the different costs that would arise with the different models and have come to the conclusion that benefit splitting, for example, is much more costly. I guess, more importantly from the government's perspective, the other models also do not address the first point I made in my opening statement that part of the government's policy aim is to deliver control to spouses through an accumulation phase.⁵¹

3.36 Participants generally agreed with the Government's view that, as proposed, option 4 was likely to be more costly. However, they considered that option 4 might be modified so that its costs to government more closely approximated those of option 2.

IFSA [Investment & Financial Services Association Ltd] proposed a simple method to limit benefits to contributions from July 2002 in the January 2002 consultations, and in a number of informal discussions with government officials since that time. We do not believe it would be difficult to limit the cost to revenue of a benefits split regime.⁵²

By restricting the amount of benefit to be split to say the post 2003 portion of the benefit, the amounts that could be split in total would be broadly similar to the Government's contribution splitting model. Thus any higher cost to revenue would only arise because of the greater likelihood of the system being used by low and middle income earners.⁵³

3.37 As noted earlier in this chapter, while option 4 in its current form may be more costly for government, it is the cheapest option for funds and fund members.

Conclusion

3.38 The Committee notes that all those who gave evidence to the inquiry supported the intent of the bill and regulations.

50 *Transcript of Evidence*, Stanhope W. pp. E30-31.

51 *Transcript of Evidence*, Murray N. pp. E35-36.

52 Investment & Financial Services Association Ltd, Submission 11, p. 3.

53 Mercer Human Resource Consulting, Submission 2, p. 5.

3.39 The Committee notes however the view of the large majority of participants that the mechanism proposed in the regulations for giving effect to this intent – annual contributions splitting (option 2) – is less likely to achieve the Government’s intentions than is option 4 – benefits splitting at the time of retirement.

3.40 The Committee further notes the serious concerns expressed by some participants about lack of clarity in the drafting of the regulations and the potential which this poses for unintended consequences.

Recommendation

The Committee recommends that the bill and regulations be agreed to.

Senator George Brandis
Chairman

**MINORITY REPORT ON THE TAXATION LAWS AMENDMENT
(SUPERANNUATION CONTRIBUTIONS SPLITTING) BILL 2003
AND ASSOCIATED REGULATIONS.**

Introduction

The Labor members of the Economics Legislation Committee do not accept the recommendation of the Senate Economics Legislation Committee that the Taxation Laws Amendment (Superannuation Contributions Splitting) Bill 2003 and associated regulations in their present form be agreed to.

Labor has some major doubts as to the advisability of any form of contributions splitting and notes, in support of that view, that there is no other retirement incomes system that permits contribution splitting.

Labor also notes that the existing family law provisions allow superannuation benefits to be split on divorce, protects the financial position of women who have not accumulated their own superannuation. It consequently cannot see any great benefit in splitting during the accumulation period, particularly given that the couple's total superannuation pool will in fact be reduced because it will be subject two sets of fees, charges and in all probability, commissions.

Given these reservations, if splitting is introduced we are of the view taken by the vast majority of the submissions made to the committee, that benefit splitting on retirement is the appropriate way to divide benefits between spouses – not contribution splitting.

We substantially agree with most of submissions that there are a number of significant reasons why option 2, the government's chosen model is costly and impracticable. In agreement with that majority it is our view is that option 4, though not without problems, is the clearly preferable option of those considered.

Disadvantages of Option 2

We agree with the central criticisms in respect of option 2 made in the majority of submissions. These objections can be summarized as follows:

The Additional Burden and Costs to Funds

The excessive costs for funds which option 2 would generate, costs that would ultimately fall on all fund members not the just the few that would benefit from contribution splitting;

The Negative Effect of Administration Costs on Superannuation Pool

The fact that the administration costs will double ultimately reducing the total superannuation pool available to the couple on retirement is a significant concern, particularly for lower and middle-income earners who will have relatively low superannuation pools that will not attract the tax benefits those with higher pools will access.

Inequitable Application of Superannuation Tax Concessions

That contribution splitting regime will result in an inequitable situation because it will largely be taken up by couples, that not only have the financial capacity to do so, but those who are informed of the tax benefits involved. These are most likely to be high-income couples with access to financial advice.

This means that those most likely to gain advantage from contribution splitting are higher income earners, not lower and middle income earners.

It should be noted that in these circumstances the impact of double fees, which will have a negative effect on a couple's superannuation pool will be of less concern to higher income earners because of the substantial tax benefits that may be obtained.

Complexity as a Disincentive

The complexity of the contribution splitting regime is such that it is likely to discourage those with lower financial literacy skills and no access to financial advice from taking advantage of the contribution splitting regime.

This would in effect act in a discriminatory way against lower and middle-income earners who are more likely to fall into this category.

Exclusion of Defined Benefit Funds

Option 4 excludes defined benefit funds meaning that a large number of members of superannuation funds will be excluded from this scheme.

Advantages of Option 4

Labor supports the arguments raised in support of the option 4 and its benefits splitting model. It agrees that benefits splitting is preferable because:

Fairer and Lower Costs

It is much fairer because the lower administrative costs of this option means that fund members will not have to carry the cost of a complex scheme that will benefit a limited few.

Greater Simplicity and Access

This options relative simplicity will result in a greater take-up particularly by lower and middle-income earners;

Consistency with Family Law

It is more consistent with the treatment of superannuation in Family Law. We are particularly concerned at the complications that the Family Law Court might face when deciding the appropriate split of superannuation benefits where previous contribution splitting has taken place.

Inclusion of Defined Benefit Funds

Defined benefit funds can be included in a benefit splitting regime whereas this option is not available to option 2.

Control by Non Contributing Spouse

It provides a spouse with control over their own share of the couple's superannuation savings, in the most important period, in the retirement phase.

Additional Concerns***Tax Minimisation***

Labor also believes that there is a risk that contribution splitting will be used for tax minimisation purposes. Although most contributors will have little hope of reaching the current RBL limits those that do, very high income people who do have the financial capacity to contribute large amounts, will do all they can to use contribution splitting to minimize tax through the access to two RBLs and two tax free thresholds.

Control of Superannuation Savings

Labor also believes that the control element argument raised in support of splitting in a minority of submissions, that is, that contribution splitting will give women some control over their retirement income savings, is largely irrelevant.

Fund members have very little direct control over funds during the accumulation period and in reality the period in which control is most important and can be fully exercised in, on retirement.

This means that benefits splitting best serves spouses who wish to have control of some of the couple's retirement income.

Discrimination against Same Sex Couples

The Bill also fails to make provision for same sex couples further perpetuating the existing discrimination against same sex couples in the superannuation system.

Government Projections and Costs to Revenue

Labor is also unwilling to support this Bill and its associated regulations while the appropriate projections that have been carried out by Treasury on the likely take up of the contribution splitting opportunity, and the cost to revenue of administering the scheme, have not been released to the public.

This is yet another example of the Government covering its actions with secrecy by keeping data that is necessary to make informed decisions concerning Australia's superannuation system out of the public realm.

It is Labor's view that the issues raised in this minority report must be addressed before any contribution splitting regime can be established.

Senator Ursula Stephens
Deputy Chair

**AUSTRALIAN DEMOCRAT SENATORS MINORITY REPORT ON
THE TAXATION LAWS AMENDMENT (SUPERANNUATION
CONTRIBUTIONS SPLITTING) BILL 2003
AND ASSOCIATED REGULATIONS**

The Australian Democrats, although not opposed to the concept of contribution splitting for couples, do not accept the recommendation that the bill and the regulations should be agreed to.

We are concerned that the implementation of the Government's Option 2 'Annual Splitting' may impose additional costs and complexity on the both superannuation industry and their members.

We are also concerned that the fees industry representatives say need to be charged (\$70-\$100) are excessive. If this option were to proceed, these fees would need to be closely scrutinised.

The intention of the legislation is to provide couples with access to two ETP thresholds and two reasonable benefit limits. However, the need to determine whether to split on an annual basis during the accumulation stage requires a knowledge of the complex tax and preservation rules within the superannuation system, along with product knowledge of applicable returns, fees and charges. We believe most Australians do not have readily available access to this information and that the costs of obtaining any advice may exceed the taxation benefits at the time of retirement.

In evidence provided to the public hearing on 25 November 2003, only one witness (Ms Pauline Smit, Women's Action Alliance) believed that Option 2 was the preferred approach, although, Ms Smit also acknowledged the need for some equity targeting to ensure that excessive benefits did not flow through to high income earners. All other witnesses expressed concerns about the administrative complexity and the possibility that the Bill would not meet the Government's objectives.

In our opinion, the Bill has significant difficulties.

As the Majority Report notes, most submissions favour an end benefit split to an annual split, and we would urge the Government to give serious consideration to this option.

We note that the Bill does not address the inherent discrimination within the Superannuation and Taxation Legislation as it applies to same-sex couples. The Democrats are committed to removing this discrimination and would have considerable difficulty supporting any legislation applying to couples that does not end this discrimination.

The Democrats reserve our position on the bill until the Government responds to these concerns.

Senator John Cherry
Australian Democrat Senator for Queensland

Appendix 1

Submissions Received

| Submission Number | Submittor |
|--------------------------|--|
| 1 | The Treasury |
| 2 | Mercer Human Resource Consulting |
| 2a | Mercer Human Resource Consulting |
| 3 | Australian Industry Group |
| 4 | The Institute of Chartered Accountants |
| 5 | Institute of Actuaries of Australia |
| 5a | Institute of Actuaries of Australia |
| 6 | The Association of Superannuation Funds of Australia Ltd |
| 6a | The Association of Superannuation Funds of Australia Ltd |
| 7 | Society of Superannuants |
| 8 | CPA Australia |
| 9 | Cbus |
| 10 | Women's Action Alliance (WAA) |
| 11 | Investment & Financial Services Association Ltd (IFSA) |
| 12 | Superpartners Pty Ltd (formerly Jacques Martin Industry Funds Administration Pty Ltd) |
| 13 | Sunsuper Pty Limited |
| 14 | Australian Administration Services Pty Limited |
| 14a | Australian Administration Services Pty Limited |
| 15 | Corporate Super Association |
| 16 | Financial Planning Association of Australia Limited |
| 17 | Mr Robert Douch |

Appendix 2

Public Hearing and Witnesses

Tuesday, 25 November 2003 Canberra

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

BAZEN, Mr Derek John, Policy Analyst, Department of the Treasury

BRADY, Ms Helen, Technical Manager, Industry Liaison, MLC

CERCHE, Mr Mark Nicholas, Chairman, Corporate Super Association

DAVISON, Mr Michael John, Technical Adviser, Superannuation,
CPA Australia

GALBRAITH, Ms Fiona Anne, Manager, Legislative Support,
Superpartners Pty Ltd

HARVEY, Mr Alan, Compliance Manager,
Australian Administration Services Pty Ltd

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

HOLLAND, Mr John, Compliance Officer,
Australian Administration Services Pty Ltd

HRISTODOULIDIS, Mr Con, National Manager,
Policy and Government Relations,
Financial Planning Association of Australia

MARONEY, Mr John, Convenor,
Superannuation and Employee Benefits Practice Committee,
Institute of Actuaries of Australia

MURRAY, Mr Nigel Patrick, Manager,
Superannuation, Retirement and Savings Division,
Department of the Treasury

QUINN-WATSON, Mr David, Member,
Regulation Subcommittee of Superannuation and
Employee Benefits Practice Committee,
Institute of Actuaries of Australia

SMIT, Ms Pauline Mary, National Secretary, Women's Action Alliance

SMITH, Ms June Marguerita, General Manager,
Policy and Regulations, Financial Planning Association of Australia

STANHOPE, Mr William George, Senior Policy Manager,
Investment and Financial Services Association

TURELLO, Ms Beverley, President, ACT Branch, Women's Action Alliance

WARD, Mr John David, Manager, Research and Information, Mercer Human
Resource Consulting