

Parliament of the Commonwealth of Australia

SENATE ECONOMICS LEGISLATION COMMITTEE

**CONSIDERATION OF LEGISLATION REFERRED TO
THE COMMITTEE**

**TAXATION LAWS AMENDMENT
(SUPERANNUATION) BILL (No. 1) 2002**

**INCOME TAX (SUPERANNUATION PAYMENTS
WITHHOLDING TAX) BILL 2002**

March 2002

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ISSN 1326-9321

Printed by the Senate Printing Unit, Parliament House, Canberra.

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Senator Mason to replace Senator Chapman on the Economics Legislation Committee until 8 April 2002.

Senator Allison substitutes for Senator Murray, for the committee's inquiry into the Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002 and a related bill.

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CONTENTS

The Committee	iii
REPORT	
Reference of Bills to the Committee	1
The Bills	1
Policy context and the proposal	1
Operation of the Bills	2
Policy intent of the Bills	2
Compliance and administrative costs associated	3
Revenue impact	3
Other implementation options considered	3
Issues raised in evidence	4
Consultation on the bills	4
Is it a new tax?	4
Are the rates of tax fair?	4
Advising people of their rights	5
Preventing fraud	5
Recommendation	6
Additional Comment by Labor Senators	7
Appendix I: Hearing and Witnesses	9
Appendix II: Consultations	11

REPORT

Reference of Bills to the Committee

1.1 Both the Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002 and the Income Tax (Superannuation Payments Withholding Tax) Bill 2002 were introduced into the House of Representatives on 14 February 2002 and the second reading was adjourned on that same day. Following a report by the Selection of Bills Committee, the Senate referred the provisions of the Bills to this Committee on 13 March for examination and report by 20 March 2002.

1.2 The Committee advertised the reference on its website and contacted the Treasury, the Australian Taxation Office, the Department of Immigration and Multicultural and Indigenous Affairs, the Australian Prudential Regulation Authority and the American Chamber of Commerce in Australia to invite comment. The Committee held a hearing on 19 March and examined officials of the Treasury, the Australian Taxation Office, and the Department of Immigration and Multicultural and Indigenous Affairs (see Appendix 1).

The Bills

Policy context and the proposal

1.3 An important component of Australia's retirement income policy is the concessional tax treatment of superannuation benefits, and the preservation of those superannuation benefits to support the retirement of Australians.

1.4 Since 1 July 1998, the preservation rules have applied to all individuals permanently leaving Australia. That is, a person who permanently departs Australia has generally only been able to access their superannuation benefits as or after they reach the eligible retirement age.¹ In contrast, before 1 July 1998 individuals permanently leaving Australia had access to their superannuation entitlements on evidence of their permanent departure.

1.5 As was foreshadowed in the Government's policy statement *A Better Superannuation System* on 5 November 2001, the current Bills propose to allow individuals who have entered Australia on certain temporary visas access to their superannuation benefits when they permanently leave Australia. These people may apply to be granted early access to their superannuation entitlements, as they do not possess the right to retire in Australia.

1.6 Accordingly, as the payments are not preserved for the purpose of retirement in Australia, the Government argues that the tax concessions that have been made available only on the basis that the funds are used for retirement in Australia should not apply. For this reason, the concessional tax treatment is recovered by making the payment of these benefits subject to a final withholding tax.

1 Prior to 1 July 1998 the preservation age for all members was 55 years but from that date a graduated scale was introduced so that for people born after 30 June 1964 their preservation age is 60 years.

Operation of the Bills

1.7 The Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002 amends the *Income Tax Assessment Act 1936*, the *Income Tax Assessment Act 1997*, the *Taxation Administration Act 1953*, the *Income Tax Act 1986* and the *Small Superannuation Accounts Act 1995* to include within the withholding tax regime the early release of payments of superannuation to certain temporary residents. The Bill does this by creating a new payment, the ‘departing Australia superannuation payment’, which will not be an eligible termination payment and will not be included in assessable income. Instead, the ‘departing Australia superannuation payment’ would be subject to a final withholding tax under the Income Tax (Superannuation Payments Withholding Tax) Bill 2002. The proposed withholding tax rates are:

- for so much of the payment as represents an undeducted contribution or post-June 1994 invalidity component – nil;
- for so much of the payment as represents an untaxed element of the post-June 1983 component – 40%; and
- for the remainder of the payment – 30%.

1.8 An alternative to this special tax (identified in the Explanatory Memorandum to each Bill²) would be to tax the temporary resident’s benefit at their marginal tax rate (adjusted for contributions tax already paid). However this approach would be administratively complex, as non-residents would be required to claim any excess tax withheld by their superannuation fund through the income tax system.

Policy intent of the Bills³

1.9 This measure will allow temporary residents who have permanently left Australia to apply to access their superannuation entitlements. These individuals would otherwise be required to leave those entitlements in Australia until they reached the preservation age, despite the fact that they have no right to retire in Australia.

1.10 This proposal is intended to reduce the administrative and compliance costs that superannuation funds incur in preserving the superannuation benefits of temporary residents who have permanently left Australia. These ongoing costs in maintaining accounts include:

- complying with the member protection rules, which require that fees charged on accounts with low balances and lost member accounts do not exceed any investment gains; and
- the administrative procedures required to be followed in attempting to contact lost members.

2 Paragraph 1.33 of the Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill (No.1) 2002, and paragraph 1.18 of the Explanatory Memorandum to the Income Tax (Superannuation Payments Withholding Tax) Bill

3 Income Tax (Superannuation Payments Withholding Tax) Bill 2002, Explanatory Memorandum, p.5. Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002, Explanatory Memorandum, p.10. Second Reading Speeches, House of Representatives *Hansard*, 14 February 2002, p. 202

1.11 Temporary resident members of superannuation funds who have permanently left Australia will benefit from a reduced likelihood that they will lose track of their superannuation savings.

Compliance and administrative costs associated

1.12 Superannuation funds would face initial compliance costs associated with changing computer systems to reflect the proposed changes.⁴

1.13 A temporary resident member who seeks to access their superannuation benefits would need to provide the fund with verification that they have met the requirements for such access. It is proposed that the Department of Immigration and Multicultural and Indigenous Affairs (DIMIA) administer the system. A fee could be charged to recover any resultant administrative costs incurred by DIMIA. The Explanatory Memorandum to each Bill notes that consideration will also be given to a more streamlined process, potentially involving accounts with very low balances.⁵

Revenue impact⁶

1.14 Government revenue will increase as withdrawals will be subject to a special tax in order to recover Australian superannuation tax concessions. The estimated revenue impact is set out in the following table (\$ million):

<i>2001-2002</i>	<i>2002-2003</i>	<i>2003-2004</i>	<i>2004-2005</i>
nil	+70	+110	+75

Other implementation options considered⁷

1.15 Other implementation options that were considered for this proposal included:

- to exempt temporary residents from the Superannuation Guarantee; and
- to allow temporary residents who have permanently departed Australia to transfer their superannuation benefits overseas.

4 Page 12 of the Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002, and page 8 of the Explanatory Memorandum to the Income Tax (Superannuation Payments Withholding Tax) Bill 2002.

5 Page 12 of the Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002, and page 7 of the Explanatory Memorandum to the Income Tax (Superannuation Payments Withholding Tax) Bill 2002.

6 Page 12 of the Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002, and page 8 of the Explanatory Memorandum to the Income Tax (Superannuation Payments Withholding Tax) Bill 2002.

7 Pages 10 to 13 of the Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002, and pages 6 to 9 of the Explanatory Memorandum to the Income Tax (Superannuation Payments Withholding Tax) Bill 2002.

1.16 The first alternative was not preferred as it was considered likely to result in labour market distortions by making temporary residents relatively cheaper to employ than similarly skilled Australians. This option would also reduce Government revenue.

1.17 The second alternative was not favoured as it would impose significant administrative costs and would not apply to all temporary residents in the same way. The second alternative may also reduce Government revenue, depending on whether the transferred amount is taxed to recover previous tax concessions.

Issues raised in evidence

Consultation on the bills

1.18 Members of the Committee inquired into the extent of consultation that the Treasury undertook in developing the bills. Officers advised that extensive consultations took place in July 2001, involving many industry and professional groups. The Treasury also provided additional information which included a list of those bodies that were consulted. This is reproduced at Appendix 2.

Is it a new tax?

1.19 Committee members asked Treasury officers whether the proposed withholding tax is a new tax. Officers characterised the measure as increasing the rate of an existing tax (the tax on Eligible Termination Payments) in the special case of departing temporary residents.⁸ The rate of tax is designed to recover previous tax concessions, reflecting the fact that the people concerned are leaving Australia permanently, and have no right to retire in Australia or to benefit from the Australian superannuation system.⁹

Are the rates of tax fair?

1.20 Committee members inquired as to the rate at which the bills proposed to apply withholding tax to temporary residents. In particular, Committee members observed that in some cases the total tax (proposed withholding tax on exit added to the previous tax on contributions), could exceed the marginal income tax that a temporary resident would have paid on the same money if it had not been paid into a superannuation fund. This is particularly the case in respect of backpackers.

1.21 Treasury officers commented that ideally the total tax rate would equal the individual temporary resident's marginal tax rate; but such an approach would be very complex to administer. Under such an approach, there would be a risk to the revenue if a temporary resident were permitted to withdraw funds during an income year in which they had no taxable income, and so faced a marginal tax rate of nil. Accordingly, the Treasury did not pursue such an approach.

8 The payment is defined as a 'departing Australia superannuation payment', but is equivalent to an Eligible Termination Payment. Taxation Laws Amendment (Superannuation) Bill (No. 1) 2002, Explanatory Memorandum, par. 1.7

9 Mr R. Cicchini (Dept of the Treasury), *Hansard*, 19 March 2002

1.22 Officers suggested that the proposed withholding tax rates represented a fair balance between equitably taxing temporary residents and recovering previous tax concessions in an administratively feasible way.¹⁰ It should also be noted that the measure is a concession to those who wish to take their benefit, and it is optional. A person who feels disadvantaged by the withholding tax always has the option of leaving their benefit in the Australian superannuation fund until preservation age.

Advising people of their rights

1.23 Committee members examined the communication strategy intended to support the proposed measure by advising temporary residents of their right to withdraw superannuation benefits when they depart. The Australian Taxation Office (ATO) advised that funding of \$4.5 million has been made available to fund a communication program during the current year targeting backpackers and other temporary residents. This could include multi-language brochures, direct mail, and advertisements in publications commonly read by backpackers.¹¹

1.24 Committee members questioned whether many temporary residents might not be aware of their superannuation benefits or which fund holds them. This is a wider issue relevant to both temporary and permanent residents, particularly seasonal or itinerant workers. The ATO foreshadowed the possibility of setting up a system by which the ATO could help applicants trace this information.¹² Mr Waters of DIMIA suggested that departing temporary residents should be readily able to find out where their superannuation benefits are held.¹³

Preventing fraud

1.25 Administrative procedures have been developed to ensure that only those entitled can access their superannuation benefits early - for example, preventing Australian citizens from accessing benefits by misrepresenting themselves as temporary residents. Draft amendments to the Superannuation Industry (Supervision) Regulations propose a two tier system.¹⁴ For accounts with a balance of \$5,000 or more, the claimant would have to provide a certificate from DIMIA. DIMIA estimates that the administrative cost of this will be about \$55 per application.¹⁵ For smaller amounts claimants would have to provide a copy of an expired or cancelled eligible visa and evidence that they have left Australia. The onus would be on the superannuation fund to have the prescribed evidence before making a payment.

10 Mr R. Cicchini (Dept of the Treasury), *Hansard*, 19 March 2002

11 Mr N. Murray (Australian Taxation Office), *Hansard*, 19 March 2002

12 Mr N. Murray (Australian Taxation Office), *Hansard*, 19 March 2002

13 Mr B. Waters (Dept of Immigration and Multicultural and Indigenous Affairs), *Hansard*, 19 March 2002

14 Draft regulations were released on 8 March 2002 for public comment. Senator the Hon. H. Coonan, Minister for Revenue & Assistant Treasurer, *Consultation on regulations to allow temporary residents access to superannuation*, press release 8 March 2002

15 Mr B. Waters (Dept of Immigration and Multicultural and Indigenous Affairs), *Hansard*, 19 March 2002

Recommendation

1.26 The Committee recommends that the bills be passed.

Senator George Brandis
Chairman

ADDITIONAL COMMENT BY LABOR SENATORS

Labor Senators note Treasury officers' evidence characterising the measures as effectively an increase in the rate of an existing tax (the tax on Eligible Termination Payments) in the special case of departing temporary residents (see report, paragraph 1.19).

While acknowledging this characterisation by the officers, it should be noted that the measures do in fact impose a new tax regime. This is evidenced by the fact that they are implemented by two bills, one to provide for the administration of the measures, the other to impose the taxation regime (as is required for tax bills). In addition, the Clerk of the Senate has confirmed that these bills do impose a new tax.

Senator Jacinta Collins
ALP Senator for Victoria

Senator the Hon. Chris Schacht
ALP Senator for South Australia

Senator the Hon. Nick Sherry
ALP Senator for Tasmania

APPENDIX 1: HEARING AND WITNESSES

Tuesday, 19 March 2002, Canberra

Department of the Treasury

Mr Raphael Cicchini - Manager Superannuation

Mr Phil Gallagher - Retirement and Income Modelling Unit

Australian Taxation Office

Mr Nigel Murray, Director, Superannuation

Mr Leon Latimore, Assistant Director, Superannuation

Department of Immigration & Multicultural & Indigenous Affairs

Mr Bernie Waters, Assistant Secretary, Business Branch, Migration and Temporary Entry Division

APPENDIX 2: CONSULTATION

The Department of the Treasury advised that during July 2001 it wrote to 24 organisations inviting formal comment on the proposal to allow temporary residents access to their superannuation. Those organisations were:

- * Association of Superannuation Funds of Australia;
- * Investment and Financial Services Association;
- * Institute of Actuaries Australia;
- * CPA Australia;
- * Institute of Chartered Accountants;
- * Australian Chamber of Commerce and Industry;
- * American Chamber of Commerce in Australia;
- * Australian British Chamber of Commerce;
- * Small Independent Superannuation Funds Association;
- * Industry Funds Forum;
- * Conference of Major Superannuation Funds;
- * Taxpayers Australia;
- * Australian Institute of Superannuation Trustees;
- * Department of Finance and Administration;
- * Department of Defence;
- * Department of Immigration and Multicultural Affairs; and
- * State/Territory authorities responsible for superannuation policy.