



13 October 2008

Committee Secretary
Senate Standing Committee on Economics
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600
Email: economics.sen@aph.gov.au

Dear Sir/Madam

Temporary Residents' Superannuation Legislation Amendment Bill 2008 and the Superannuation (Departing Australia Superannuation Payments Tax) Amendment Bill 2008

Thank you for the opportunity to comment on these Bills which were introduced into Parliament on 25 September 2008.

Executive Summary

Following on from the discussion paper released earlier this year, it is pleasing to see that the Government has responded favourable to many of the serious concerns raised by Mercer and others in the industry. These Bills resolve many of the issues we identified, however, a number of concerns remain:

1. The retrospective nature of the changes/tax increases
2. The additional reporting requirements on funds and the timing of implementation
3. There appears to be no requirement for the ATO to provide ongoing information to former temporary residents on the status of their account.

We also note that these changes are likely to make it more difficult and more expensive for employers to recruit skilled temporary residents. In some cases, current temporary residents may decide to leave Australia earlier than otherwise planned in order to avoid the higher proposed tax rates.

We have recommended that:

- Former and current temporary residents be exempt from the new legislation with the provisions only applying to future temporary residents



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- The rate of tax on Departing Australia Superannuation Payments should be retained at 30% rather than being increased to 35%
- Where a person has satisfied another condition of release (such as retirement, death invalidity etc), the same rate of tax as applicable to Australian residents should apply rather than the rate applicable to Departing Australia Superannuation Payments
- Implementation should be deferred by at least 6 months to enable superannuation fund trustees to implement appropriate procedures and systems changes and to provide greater opportunity for contact to be made with members affected
- The ATO should provide annual benefit statements of amounts held.

Who is Mercer?

Mercer provides consulting and administrative services to a significant number of superannuation funds (including industry plans, master trusts, corporate funds and government sector funds) as well as to employer clients. We also provide our own master trust which currently has approximately \$13 billion of assets. Our financial planning business provides advice to individuals whilst our Human Capital business provides advice to employers in relation to workforce planning issues etc.

We also employ a number of skilled temporary residents who are quite concerned about the implications of these Bills.

We are therefore well placed to comment on the proposals from the various perspectives of a superannuation provider/trustee, employer and employee.

Detailed Comments

The major changes that will result from these Bills are:

- (a) when a temporary resident has left Australia for a period of more than 6 months, the ATO will require the person's superannuation fund to transfer the member's benefit to the ATO where it will earn no interest
- (b) the tax payable on the benefit when it is paid to the person (either directly by the fund or by the ATO) will increase from 30% to 35% if paid as a Departing Australia Superannuation Payment or from 0% or 15% to 35% if the person had satisfied a retirement condition of release, died or become permanently incapacitated etc before claiming the benefit.



1. The retrospective nature of the changes/tax increase

If passed in its current form, the Bill will have an adverse retrospective impact on both current temporary residents and many former temporary residents who have already left Australia but not yet claimed their benefit. The retrospective nature of the proposed changes is a significant concern.

Whilst some former temporary residents may have forgotten their Australian superannuation entitlements, many such former residents have deliberately chosen to leave their superannuation savings in Australia. Under current legislation (ie the legislation which existed at the time they left the country) they expected that their benefit would continue to grow with investment earnings and that they would eventually be able to take their benefit on retirement at the normal Australian tax rates applicable to superannuation benefits.

Under the provisions of the Bill, these former temporary residents will either:

- have to cash their benefit under the DASP provisions before their fund is required to transfer the benefit to the ATO (paying tax of either 30% or 35% depending on the timing); or
- find that their benefits have been transferred to the ATO earning 0% interest and will be taxed at 35% (a much higher rate than they would have expected under the existing legislation).

We note that these former residents may be difficult to contact and may therefore not become aware of these significantly adverse changes for many years. Further, superannuation funds are unlikely to know whether any of their members are former temporary residents and will therefore have difficulty in preparing any targeted communication to advise them of the changes.

Current temporary residents will now also be subject to a higher rate of tax and will not be able to leave their benefits in existing funds for more than about six months when they depart. These current residents have already made contribution decisions based on current legislation. They will have no option but to pay significantly more tax on their eventual benefit than was expected when the contributions were made.

Under the proposed provisions, the combination of contribution tax and tax on the benefit will result in most temporary residents paying higher tax on their superannuation than if they had taken additional salary instead of their superannuation.



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Of particular concern is the new tax treatment of temporary residents who had planned to leave their benefit in an Australian fund until after age 60. Currently, existing benefit payments to those over age 60 are tax free.

As indicated above, these people have made decisions about contributions, insurance and investment issues based on the current laws and rates of tax. For example, they may have made those decisions on the understanding that their benefit will be tax free when taken from age 60 and that their benefits would continue to grow with investment earnings until that date.

We also note that in at least some cases, any Australian superannuation benefit received after leaving Australia may also be subject to tax in the person's country of residence. Australia's double tax agreements with other countries generally do not apply to lump sum superannuation benefits. These members may therefore not only be subject to the Australian taxes of 15% on contributions and investment earnings and 35% on the benefit, but may also be subject to further tax in their home country.

Retrospective treatment can generally be avoided by either exempting those adversely affected from the retrospective provisions or by at least quarantining amounts which had accrued up to the date of the changes. We consider that in this case, quarantining accrued amounts or applying some form of pre and post formula would be far more expensive to implement and administer.

Recommendations

- We consider that, because of the retrospective treatment involved, these proposals are inappropriate for those former temporary residents who have already left Australia and for current temporary residents. The provisions of the Bill should not proceed for these groups. Any changes should be restricted to future temporary residents. Quarantining existing amounts (or applying a pre and post formula) is likely to be significantly more costly for superannuation funds to administer and is not an appropriate option.



- If the changes do proceed in respect of former temporary residents, then the implementation date should be deferred. This would provide some opportunity to contact this group to advise them of the forthcoming changes and at least giving them an opportunity to act before the changes and increased tax rates come into force. However, superannuation funds will not be able to provide such information unless the ATO provides them with lists of former residents that might be members of each fund.
- We also consider the plan to tax former and current temporary residents at the full 35% rate inappropriate where these former residents have, at the time they claim their benefit, met another condition of release (eg retirement, death, terminal medical condition, invalidity etc). For example if a benefit is paid by the ATO to a person who has met such a condition, the same rate of tax as applies to Australian residents should apply. (For example, no tax would generally apply where benefits are claimed after age 60.)
- The 35% tax rate is too high taking into account the level of contribution tax and possible taxes imposed by the former temporary resident's home country.

2. Timing of Implementation

We have mentioned above that consideration to delaying the introduction of these changes would assist contacting former and existing temporary residents to give them the opportunity to make other arrangements.

We also have concerns regarding the industry's ability to implement the changes and meet the proposed first lodgement date of 30 April 2009.

Firstly, it is unreasonable to expect trustees to implement system changes before the legislation is finalised. We expect that there will be only limited time after the legislation is passed before the first lodgement date. Whilst many funds will not have many former temporary residents, proper systems still need to be in place to enable efficient processing.

The new requirements will be particularly difficult for funds with a high number of former temporary residents. There may be considerable difficulties in determining the appropriate amounts to transfer and trustees may have difficulty in obtaining sufficient cash to make the payments in a short space of time without unduly impacting on the fund's short term investment strategy. Due to their nature, we expect that Eligible Rollover Funds will be one group of funds that may be particularly exposed to these changes.



Recommendation

- We recommend that the commencement date for the legislation be delayed by at least 6 months to ensure sufficient time for superannuation fund trustees to alter their systems and procedures and to contact former and current temporary residents to advise them of the changes. This will also give employers more time to take into consideration these changes when determining employment contracts for future temporary residents.

3. Ongoing information to former temporary residents with money held by the ATO

If the management of the accounts of former temporary residents is to be transferred to the ATO, we would expect the ATO to provide members with annual benefit statements (that will show that no interest has been credited) as a reminder to former temporary residents who are yet to act.

Recommendation

- The ATO should provide an annual benefit statement to former temporary residents where contact details are known.

Technical issue

There appears to be an inconsistency between the Bill and the Explanatory Memorandum.

Proposed Section 20F of the Superannuation (Unclaimed Money and Lost Members) Act 1999 sets out the calculations involved in determining how much a superannuation fund must pay to the ATO. Sub-section (3) indicates that the payment can be reduced by any amount that the SIS Regulations require **or permit** to be cashed.

The Explanatory Memorandum (Paragraph 1.44) indicates that this is only possible where there is a **requirement** on the provider to pay that amount.

This inconsistency needs to be clarified to avoid subsequent confusion for trustees who will be required to calculate the amount to be transferred.



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Example: Erik is a temporary resident who has left Australia. The trustee of Erik's superannuation fund is aware that Erik has satisfied an invalidity condition of release. It is therefore **permitted** to pay that benefit. However it is not **required** to pay the benefit unless Erik requests payment.

Erik has not requested payment and currently cannot be contacted.

Section 20F implies that some or all of the benefit will not need to be transferred to the ATO. Based on the Explanatory Memorandum, the whole benefit would need to be transferred and would be taxed at a significantly greater extent than if the benefit could be paid directly to Erik.

Labour and Skills Shortage

Many Australian businesses are having difficulty in recruiting appropriate skilled staff. The recruitment or transfer of employees from overseas is one means of solving these shortages.

In the light of these shortages, we question whether the proposed changes in relation to temporary residents' superannuation are sending an appropriate message to employers and those considering coming to work in Australia for a short period.

Please contact me on 03 9623 5552 if you have any queries.

Yours sincerely

A handwritten signature in blue ink that reads 'John Ward'. The signature is written in a cursive, flowing style.

John Ward
Manager, Research and Information