

Appendix 13

Grandfathered/sunset provisions relating to taxation of superannuation

Introduction

This appendix summarises the grandfathered/sunset provisions relating to the taxation of superannuation. It reproduces Attachment C of the supplementary submission of the ATO to this inquiry.¹

Eligible termination payments

The position prior to 1 July 1983:

- Prior to 1 July 1983, only 5% of certain lump sum benefits, including superannuation, were included in the recipient's assessable income and taxed at marginal rates.

The position after 30 June 1983:

- From 1 July 1983, the term eligible termination payment was introduced and effectively apportioned certain lump sum payments made on retirement, and termination from employment over the eligible service period (ESP) between pre-July 1983 and post-June 1983 service (or fund membership).
- The measures were aimed at encouraging taxpayers to save for their retirement by deferring taxation on their payments through the introduction of roll-over funds. By rolling-over a payment into an Approved Deposit Fund (ADF), a taxpayer was able to defer payment of tax on the payment. Subsequent withdrawal of the payment at or after age 55 resulting in more generous tax concessions becoming available.
- The result of these changes was that, five per cent of the amount identified as the pre-July 1983 component continued to be assessable at the taxpayer's marginal rate and the post-June 1983 component became fully assessable. The rate of tax payable on the fully assessable amount can range from 0-30 per cent depending on the source of the payment, the ESP and the age of the recipient.

Note: If a Tax File Number (TFN) is not supplied, the payment may be subject to the highest marginal rate of tax.

1 *Submission 148, ATO, Attachment C.*

The position after 30 June 1988:

- As a result of the then Treasurer's May 1988 Economic Statement, a tax on the earnings of superannuation funds was introduced. This tax meant that superannuation funds, ADFs and life organisations which had previously been virtually free from tax, would be taxed on their earnings.
- The rate of tax was 15 per cent for funds which complied with the relevant legislation and the highest marginal rate for those funds which did not comply.

Concessional component:

- The concessional component of an ETP is that part of an ETP which was made before 1 July 1994 and was attributable to a bona fide redundancy payment, approved early retirement scheme payment or an invalidity payment.
- Only five per cent of the concessional component is included in the taxpayer's assessable income and taxed at marginal rates.

Post-30 June 1994 invalidity component:

- From 1 July 1994, an invalidity payment (previously included as a concessional component) is included as part of an ETP as the Post 30 June 1994 Invalidity component.
- This component is tax free to the payee and can be rolled-over.
- The post-June 1994 invalidity component of an ETP that has been rolled over to purchase an annuity or pension forms part of the UPP of the annuity or pension.

Undeducted contributions:

- Undeducted contributions represents the amount of contributions paid by an individual, or by any other person (other than an employer of the person), to a superannuation fund after 30 June 1983.
- Undeducted contributions are not included in the taxpayer's assessable income, ie they are tax free.

Non-qualifying component:

- This ETP component commenced from 1 July 1985.
- A non-qualifying component arises as a result of the commutation or residual capital value of an immediate annuity which was purchased partly with non-ETP money.
- The non-qualifying component is the part of the ETP that represents investment income accruing between the time of purchasing the annuity and the time of the payment.
- The amount is included in assessable income and is subject to the taxpayer's marginal rate of tax. The non-qualifying component cannot be rolled-over.

Excessive component:

- The excessive component of an ETP is the amount of the ETP which the Commissioner has determined to be in excess of the individual's RBL.
- Any excessive component of an ETP is fully assessable and taxed at the top marginal rate of tax. This is regardless of the taxpayer's level of income. Prior to 1 July 1994, the excessive component was taxed at the taxpayer's marginal rate.
- Where the person receiving an ETP fails to provide the payer with their tax file number the total amount of the payment will be treated as an excessive component.

Reasonable benefit limit

There is a limit to the value of these benefits that a person can receive over their lifetime at reduced tax rates. This limit is called the RBL. RBLs were introduced to prevent excessive exploitation of the concessional tax rates accorded to these payments, and to provide a more equitable distribution of these tax concessions.

RBLs are therefore the maximum amount of retirement and termination of employment benefits that a person can receive at concessional (reduced) tax rates over their lifetime.

Prior to 1 July 1985:

- any benefits paid by superannuation funds had to be reasonable in accordance with a scale based on the member's salary. Funds that breached this rule, lost their tax exempt status as complying funds were tax exempt at this time.

1 July 1985 to 18 December 1987:

- The ATO determined if benefits were reasonable using Income Tax Ruling 2201 (IT2201).

18 December 1987 to 30 June 1988:

- The Insurance and Superannuation Commissioner administers RBLs still applying IT2201.

1 July 1988 to 30 June 1990:

- The May 1988 Economic Statement included:
 - a new RBL salary scale;
 - a review of administrative arrangements; and
 - Insurance and Superannuation Commission (ISC) Circular replaces IT2201.

1 July 1990 to 30 June 1994:

- *Occupational Superannuation Standards Act 1987* (OSSA) and *Occupational Superannuation Standards Regulations* (OSSR) amended to include RBL legislation (Part IIIA) RBL regulations (Part 1A). RBLs based on Highest Average Salary (HAS) and Eligible Service Period (ESP).

29 May 1993 to 30 June 1994:

- ATO administers RBLs under delegation from the ISC.

1 July 1994 to present:

- The ATO takes over from the ISC the administration of RBLs. *The Income Tax Assessment Act 1936* (ITAA) and *Income Tax Regulations* (ITR) amended to include the RBL legislation (Part III, Div 14), and RBL regulations (Part 5A). The HAS-based system of calculation for RBLs was replaced by flat dollar limit RBLs with effect from 1 July 1994. Although fixed amounts were introduced as RBLs from this date to all individuals regardless of the level of their HAS, the HAS-based method of RBLs did not become obsolete because it applied in calculating a person's Transitional RBL.
- Transitional RBLs were introduced at the same time as flat dollar limits to minimise any disadvantage created through any possible reduction of an individual's RBLs resulting from the new legislation. It provided a means for protecting individuals who had made their retirement plans based on the previous system by allowing them a greater RBL than the new flat dollar limits.
- The eligibility for a TRBL is determined in accordance with the age of the person as at 1 July 1994. The various categories are:
 - individuals aged under 45 years on 1 July 1994 (born after 1 July 1949);
 - individuals aged at least 45, but under 50 years on 1 July 1994 (born after 1 July 1944 and on or before 1 July 1949); and
 - individuals aged at least 50 years on 1 July 1994.
- Individuals who wished to have a TRBL registered had to apply for one in the prescribed manner by the 31 December 1996. This date was subsequently extended to 4 April 1997. Under the *Income Tax Regulations* a taxpayer may request the Commissioner to register their TRBL's at later time (AAT Case AT1999/49).

ITAA 1936 Part IX Taxation of Superannuation and Related Business***Pre 1 July 1998 funding credits:***

- Complying superannuation funds previously exempt from income tax until 30 June 1988 may exclude employer contributions from their assessable income if the contributions relate to unfunded liabilities accrued up to 30 June 1988. (Ref s 275A & 275B ITAA 1936).

Increased death benefits:

- A fund is able to claim a deduction, the benefit of which is passed to a death beneficiary, so that the death benefit amount is not reduced because of tax on contributions. (Ref s 279D).

Amounts accrued before 1 July 1988:

- Income accrued to a complying superannuation fund before 1 July 1988 but derived after that date is not included in assessable income. (Ref s282 ITAA 1936).

Taxation of annuities and pensions

An annuity or pension that commenced before 1 July 1983:

- Assessed under former section 26AA (as opposed to section 27H). This gives rise to some differences when calculating the deductible amount for the pension or annuity, particularly when the pension or annuity reverts to a death beneficiary.

A pension commencing after 1 July 1994:

- When a pension commencing after 1 July 1994 is purchased wholly with roll-over amounts arising from the commutation of pensions or annuities which commenced before 1 July 1994, the more generous calculation of the related undeducted purchase price (which applied before 1 July 1994) applies to the new pension or annuity. (Ref s27AAAA ITAA 1936)

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