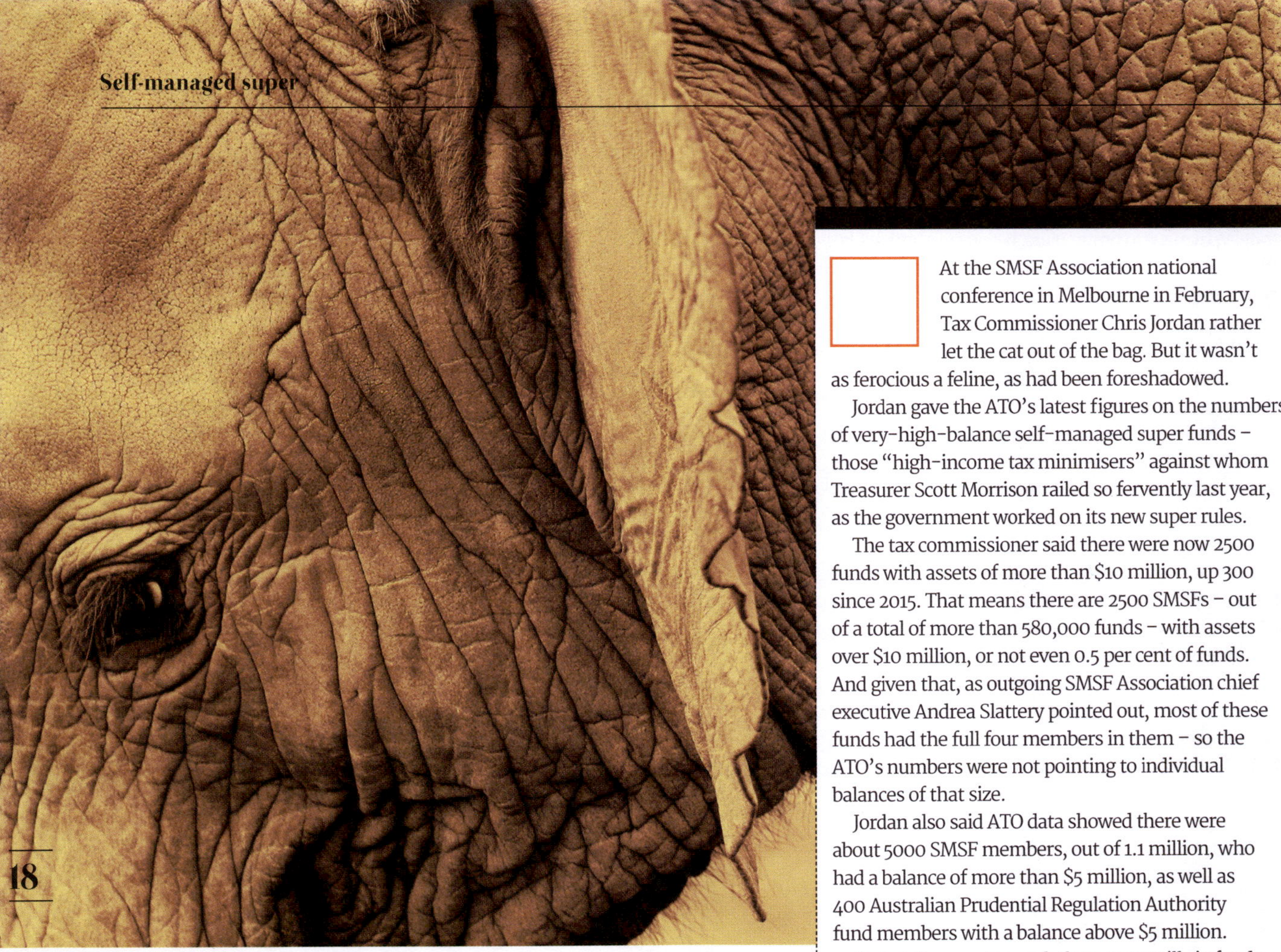

WORDS JAMES DUNN

AN ENDANGERED SPECIES *AFFECTING POLICY*

MEGA-SMSFS ARE A PRODUCT OF LAWS THAT ARE ALREADY EXTINCT BUT THE GOVERNMENT STILL APPEARS TO HAVE ITS EYE ON THEM. THE AIST THINKS THIS HAS LED TO A LAYER OF COMPLEXITY IN THE LAW THAT COULD BE REMOVED.

At the SMSF Association national conference in Melbourne in February, Tax Commissioner Chris Jordan rather let the cat out of the bag. But it wasn't as ferocious a feline, as had been foreshadowed.

Jordan gave the ATO's latest figures on the numbers of very-high-balance self-managed super funds – those "high-income tax minimisers" against whom Treasurer Scott Morrison railed so fervently last year, as the government worked on its new super rules.

The tax commissioner said there were now 2500 funds with assets of more than $10 million, up 300 since 2015. That means there are 2500 SMSFs – out of a total of more than 580,000 funds – with assets over $10 million, or not even 0.5 per cent of funds. And given that, as outgoing SMSF Association chief executive Andrea Slattery pointed out, most of these funds had the full four members in them – so the ATO's numbers were not pointing to individual balances of that size.

Jordan also said ATO data showed there were about 5000 SMSF members, out of 1.1 million, who had a balance of more than $5 million, as well as 400 Australian Prudential Regulation Authority fund members with a balance above $5 million.

And at the very top end, there were still six funds with balances over $100 million. But these SMSFs – which have family-office-style firepower – are accidents of history and past legislation.

FROM DAYS GONE BY

"Those SMSFs on the larger size put things in there a long, long time ago and locked it up – they had sufficient funds at the time and were willing to lock up that money for decades and it did grow, and they tend to be people in their 80s," Jordan told the SMSF Association conference.

These mega-funds represent "a problem that will literally die out," says Jordan George, head of policy at the SMSF Association.

"There are very few really large SMSFs, and they are very much a product of people who made significant contributions before the current limits applied, and also were fortunate enough to invest very well. It's no longer possible to accumulate such large balances under the more recent set of rules, and we won't see their like again," George says.

A MISCONCEPTION GUIDING POLICY?

Despite this, the government clearly fixated on the mega-funds as it went about deciding on the new rules.

"When Australians see the government supporting the accumulation of enormous superannuation fund balances in a tax-preferred (and in retirement, tax-free) environment, that does undermine confidence in the system," Morrison said in November 2015. "Super should not be seen as an open-ended savings vehicle for Australians to accumulate large super balances in a tax-preferred environment, well in excess of what is required for an adequate retirement. It is not an estate planning vehicle, nor was it ever intended to be," he said.

The mega-funds go well beyond what the government is talking about in terms of the objective of superannuation – its legislation describing super's purpose as "to provide income in retirement to substitute or supplement the age pension" is being reviewed by a Senate inquiry.

"The government has made it very clear, and this is still its position, that superannuation is not a wealth-creation vehicle. You can look at these very large funds and they are a very obvious target of that kind of talk, and I think those funds have had anecdotal influence on the SMSF sector over the years," George says.

A misconception has definitely arisen about the SMSF sector, he says, that huge funds are common.

"From our point of view, it has been great to see the tax commissioner clarifying the actual numbers, and showing that we're really only talking about a very small number of funds," George says. "We think the important point to take from the ATO's figures is that SMSFs are really not a vehicle for the super-rich to shelter assets from tax."

What's more likely, George says, is that the government has targeted its policy at SMSFs with balances of about $2.5 million.

"We think that level of fund has had a greater influence on the policy. This has been a far further-reaching package in trying to limit the concessionality for super on contributions than what we've seen before; but also limiting the concessions for large balances in retirement – which is something we haven't really seen before [either].

"That's probably where this idea of large SMSFs plays into that policy. It affects these funds that have significant individual-member balances of $1.6 million and over, funds that have a minimum $2 million-$3 million of balances, that's where the $1.6 million cap starts hitting SMSFs. There are a lot more of them than there are funds in the $10 million-and-over range," he says.

Anecdotally, he says, the idea of large funds has swayed the debate on super over time, but the government has "left them alone" in the new legislation.

"The government knows they will be picked up in the new measures. They've set a lower level to try to put a cap on the future ability to get open-ended tax concessions in the retirement phase. No matter what your balance is, concessionality is limited to $1.6 million," George says.

The latest changes will have "little or no impact" on the majority of Australians, for whom $1.6 million in super is "an impossible dream," says Robert MC Brown, former chartered accountant and financial adviser, and chairman of the ADF Financial Services Consumer Council.

"I do think policymakers were seeking to curtail the growing view of superannuation as a wealth accumulation strategy to enable relatively wealthy Australians to leave large amounts of tax-protected money to their children, rather than building up a nest egg for the current generation to extinguish in retirement," Brown says. "But we're talking here about tax concessions for relatively wealthy people – although some of them probably don't feel all that wealthy."

Looking at the distribution of the super tax benefits, the wealthy get a benefit that is "some multiple of the benefit" that is attained by other Australians, says David Haynes, executive manager, policy and research, at the Australian Institute of Superannuation Trustees (AIST).

WHERE TO STRIKE A BALANCE

"The confluence of super being tax-free over age 60, which is not means-tested prior to this measure, and fairly generous limits on non-concessional contributions until recently, has [created an] opportunity for the very wealthy to transfer very high levels of assets into superannuation. That hasn't been closed down, but a ceiling has been put on it. The $1.6 million transfer balance cap and the $1.6 million cap on non-concessional contributions provide that ceiling," Haynes says.

The AIST believes the transfer balance cap should have been set higher, Haynes says, and the complicated indexation requirements discarded. The transfer balance cap is indexed in increments of $100,000 on an annual basis, in line with the Consumer Price Index (CPI): a person's eligibility to receive indexation increases in relation to their personal transfer balance cap and is subject to a formula based on the highest balance of the member's transfer balance account compared with the member's personal balance cap.

"With the way that the indexation requirements are structured, it basically means that there needs to be an alternate record-keeping system – maintained by the ATO – in relation to everyone who is in retirement phase, even though the vast majority of people won't be [affected] by it," Haynes says. "We think the implementation transition – and its ongoing management – will add a layer of complexity to what is already a fairly complicated area of the law."

The AIST states that instead of having a $1.6 million cap and this complicated indexation arrangement, the ceiling could simply have been set higher. "We think it could have been set at $1.7 million, for example. If that meant that, yes, very rich people could then sneak another $100,000 into super, so be it," Haynes argues.

George says the bottom line that should be remembered is that no matter what your super balance is, concessionality is limited to $1.6 million – but even above that, a 15 per cent tax rate is still concessional.

"Superannuation is still a great deal when it comes to tax treatment in retirement, even if taxed at 15 per cent.

"That's still a great tax-effective vehicle, and it's a very strong incentive to keep your money in super, for tax-free earnings in retirement. Even if you go over the $1.6 million limit, you still have an excellent opportunity," he says. "If you were sitting in a $10 million fund, you'd still want to err on the side of keeping your money in the super system, because of the great concession that 15 per cent tax on earnings represents." ■