15 September 2017

Kasey Macfarlane
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Australian Tax Office

Email: Kasey.Macfarlane@ato.gov.au

Dear Ms Macfarlane,

SMSF ASSOCIATION SUBMISSION ON AUSTRALIAN TAX OFFICE'S TRANSFER BALANCE CAP & SMSF 'EVENT-BASED' REPORTING FRAMEWORK POSITION PAPER

The SMSF Association (SMSFA) welcomes the opportunity to make a submission regarding the Australian Tax Office's (ATO) Transfer Balance Cap and SMSF 'Event-Based' Reporting Position Paper. We endorse the ATO's endeavour to allow for consultation and feedback in order to facilitate a practical approach to the implementation of the Transfer Balance Account Report (TBAR) across the superannuation industry.

We also understand that the proposed reporting standards will eventually require all self-managed super funds (SMSFs) to lodge a TBAR no later than 10 days after the end of the month in which a relevant reporting event occurred in line with other superannuation funds. Shifting pension reporting to an event-based approach from the current annual method is a significant change for the superannuation system, especially for SMSFs.

The SMSFA supports the intention to provide administrative concessions for SMSFs to support their transition to event-based transfer balance cap (TBC) reporting.

Event-based reporting is a substantial shift from the current reporting arrangements and we suggest caution in its design and final implementation. Event-based reporting has the potential to significantly increase the compliance burden on SMSF trustees and their advisors, even when they are not affected by the TBC rules (i.e. they are well under the $1.6 million TBC limit). Accordingly, how reporting is designed and what compliance approach the ATO takes will have a significant effect on the SMSF sector.

It is essential that TBAR administration allows an appropriate transitional period and is also fit for purpose to ensure the minimum disruption possible.

Preferred transition approach

The SMSF Association supports 'option 2' in the ATO's Position Paper which will mean that from 1 July 2018, SMSFs will have 28 days after the end of the relevant quarter to report all TBC events except commutation authorities and commutations after an excess transfer balance tax determination. After an agreed upon transitional period, SMSFs will then be required to report all events monthly.

We believe that option 2 will allow for a smoother transition to event based reporting as trustees and their advisors will have more time to ensure that reporting obligations are met after a relevant TBC event has occurred. The SMSFA has surveyed its membership and over 90% of respondents were supportive of option 2 in the ATO's Position Paper.

We also relay the following relevant results of our member survey to the ATO:

- Less than half of the respondents are currently ready for the ATO's introduction of event-based reporting.
    - In turn, less than half are satisfied with the intended start time.
- Only half of respondents understand the intent and what is required to satisfy ATO's event-based reporting.
- There is general concern about SMSF advisors' ability to cope with the significant amount of changes in the superannuation environment and increased costs for clients driven by extra requirements.
    - This broad message is expanded upon throughout our submission.

Option 2 and the proposed transition period

The SMSFA is supportive of option 2, as this option provides the easiest form of administration for SMSF trustees and advisors in the transition to event-based reporting. Rather than having different process for different events, it will help the creation of processes for the industry that are consistent to implement and further help a transition to monthly reporting. This will allow SMSF advisors to more easily transition their systems to monthly reporting when the transition period ceases.

Incorporating monthly reporting events from 1 July 2018 would have placed an unnecessary burden on SMSF trustees and advisors. The industry needs an extensive period of transition to ensure quarterly reporting is effective before an introduction of different reporting timeframes. Software providers and advisors need to ensure their platforms and firms have set up the appropriate processes and systems to first cope with transitional reporting and then more frequent monthly reporting. It is a common theme throughout the SMSF industry, and evidenced in our survey of members, that the industry is currently overwhelmed with the superannuation changes taking effect from 1 July 2017, the introduction of the licensing regime for accountants and the usual ongoing compliance requirements. Accordingly, flexibility from the ATO is essential at this time to ensure that the impact of the increased compliance obligations brought about by the TBC and event based reporting is minimised.

In this context, the SMSFA currently has no immediate concerns with the proposed two year transition period up until 1 July 2020. From this date, it is understood that all events should be reported 10 days after the end of the month in which they occur. However, we believe that the ATO should undertake consultation with the SMSF industry in early 2020 to understand the readiness of the sector to shift to monthly reporting. This will give the ATO the knowledge and flexibility to determine whether an extension of the transition period is warranted. If the industry was not is a state of readiness for monthly reporting due to unforeseeable circumstances such as problems engaging trustees, increased costs and system design failure we would expect that this transition period can be extended.

Concerns with the ATO ability to maintain and consolidate TBAR data given advisors experience with ATO portal failures

Given recent failures with the ATO tax agent portal it is also essential that the ATO has the ability to maintain and consolidate the TBAR data as well as provide access to it for SMSF trustees and their advisors. It is imperative that the amount of data the ATO will receive from the TBAR is not underestimated. Therefore, clear information should be provided to the industry about how they should report, where to report and when to report as soon as possible. This involves clear communications, screenshots of the design of the TBAR portal and potentially increased web-content and webinars.

The ATO should also be certain that its systems are ready before moving into the transitional and final event-based reporting stages. Given the sensitivity in the introduction of this regime, there will be an enormous amount of angst and goodwill lost if SMSF trustees and advisors are ready to report and the TBAR system cannot handle and provide data to the industry. Further, SMSF advisors and trustees will be reliant on the ATO for the provision of live information back to them and this must be ready.

Therefore, it should be considered, at the appropriate time if the TBAR portal is not ready, that the reporting period commencement date (1 July 2018) be delayed until such time as it is. This will place the burden of reporting to be kept by SMSF advisors and trustees but they will be able to control this information and their annual reporting sufficiently until the portal is ready.

Increased monitoring of all client pensions regardless if they are nearing the $1.6 million TBC

A common theme emerging from our members has been the query on why all client pensions need to be reported on regardless if they are nearing the $1.6 million TBC. Given that a member with a superannuation balance below $1 million for example does not have any immediate issues regarding compliance with the TBC, it may be construed as over-regulation and an unnecessary compliance cost. This is further exacerbated by the fact that SMSF members with smaller balances may be exposed to larger administration costs in a cost-to-assets ratio sense in the early years of the event-based reporting implementation.

The SMSF Association proposes that the ATO consider looking into the feasibility of amending this requirement for the proposed transitional period. For example, members with a total superannuation balance below $1 million could be carved out of reporting until 1 July 2020 (the end of quarterly transition period). This would have the added benefits of:

- Reducing compliance strain on SMSF trustees and advisors in the immediate future.
- Result in minimal revenue leakage from SMSFs.
    - Their pensions will be reported on an annual basis in the Superannuation Annual Return.

- Reducing the data burden on the ATO's systems and portals while the TBAR is being implemented in its transitional stage.

Amount of reportable events

The SMSFA believes there needs to be a greater recognition of the impact regarding the amount of reportable events. Views which dictate that individuals may have two reportable events in their lifetime are overly simplistic and all parties must come to an understanding of the practical implications in order to ensure a seamless transition. We note some common scenarios:

- Despite only 48% of SMSFs being in retirement phase and therefore event-based reporting not affecting everyone initially, firms will need to ensure systems are set up across their entire client base. This should come into consideration when determining an appropriate transition period.
- Commutations from pension accounts will largely increase due to the introduction of the TBC and the 'debits' that arise. We envision all payments above the minimum pension amount will be taken first as lump sums from remaining accumulation accounts, and then as lump sum commutations from pension accounts, giving rise to a TBC debit. Prior to the introduction of the TBC there was minimal need for SMSF trustees to engage with their advisor on such a regular occurrence regarding withdrawals to enable funds to appropriately report.
- It is a common industry practice to commute and recommence pensions at the start of every financial year to 'sweep' up any additional contributions that have been made during the year. Therefore, despite having 'one' pension throughout their life, this will create additional reporting events.
- It is very likely for most SMSF members to have more than one income stream for a variety of strategic reasons. This will further add to the complexity in data monitoring and ATO systems. This must be taken into account in the design of the TBAR.

Valuations and estimates

No matter which option is chosen, the commencement of a retirement phase income stream will need to be reported to the ATO 28 days after the end of the quarter in which the income stream commenced. For the common 1 July commencement, this will be on 28 October. As SMSFs generally align the valuation of their assets with the completion of the fund's end of year financial accounts, it is very possible that funds will not have the exact value of their income stream by this date. This is made difficult by the fact that taxation statements, asset valuations and SMSF documentation are not usually received by advisors by this date. This is a pertinent issue that needs well-defined clarity from the ATO.

Appendix D of the Position Paper currently details the ATO's position regarding valuations. It details that SMSFs should continue to apply the ATO's valuation guidelines for SMSFs where income streams commence part way through an income year. It states:

'It is accepted that a reasonable estimate of the value of the account balance can be used when a pension is started part way through the year'

This should be clarified to specify that this should apply to all income streams no matter when they are commenced. Given that accurate valuations are not likely to be obtained by 28 October for 1 July commencements, a reasonable estimate will still be needed at this date.

Consistent with these guidelines, the ATO is accepting a 'reasonable estimate' of the starting value of a retirement superannuation income stream. The ATO also states this value should be recorded in the funds accounting reports and in the TBAR.

Given this requirement, the following should be clarified:

- When further accurate information is received, can and should an SMSF trustee go back and amend these valuations?
    a. Is the ATO position that the 'reasonable estimate' must be reflected in the financial reports for the financial year even when further information is received and that the TBAR should not be adjusted?

       OR

    b. Is that the ATO position that the 'reasonable estimate' can be adjusted in the TBAR when further information is received to match the final SMSF financials?

When final financial reports are prepared, it is our experience that there will likely be a discrepancy between any prior estimate valuation and final valuation.

With the preparation of interim accounts costly and an administrative burden for SMSF trustees and accountants, we strongly support the use of a 'reasonable estimate' and support that SMSF trustees should not go back and amend these valuations. This may be variation from normal protocols.

We believe for simplicity, that the reasonable estimation should be final for all TBAR reports and financial reports. This will allow the TBAR to match up with the financial reports and the SMSF Annual Return.

Other issues to be clarified are:

- What are the options available to amending a reported TBAR? Under what circumstances is this allowed and if so, how many times?

- From an administrative perspective, it is unclear what happens when there is a reporting error that has affected a member's TBAR? How does the member identify whether it is a fund reporting problem or an ATO processing problem? Where there are multiple funds, how do they know which fund may have misreported? It is most likely that on receipt of an excess determination a member will engage their accountant/adviser to resolve and this will put further pressure on recoverability of costs, especially where a third party is at fault.

Reporting multiple income streams

The SMSFA understands that to ensure accuracy of data the ATO needs to collect what type of income stream a member is commencing. However, given that the majority of SMSFs can and only pay account based pensions (ABPs), we question why there is a need to track every ABP independently, rather than at the member level. Given that there is no different impact on the TBA, that is, the total credit to the TBA is the relevant number whether made up of one or multiple ABPs, there may be no material difference.

As it is common practice for trustees to establish multiple ABPs in an SMSF we believe there is an opportunity to reduce red-tape by adopting a member reporting framework for ABPs which can be complemented by member benefit statement reporting.

Relief for small excesses on 1 July 2017

The TBC legislation has provided special transitional rules for individuals with TBAs between $1.6 million and $1.7 million from 1 July 2017 for six months. During this period, trustees will have time to remove the excess from retirement phase without penalty.

This does not seem to be stated in the Position Paper.

Penalties

The SMSFA believes that there should be some information regarding the penalty system for event-based reporting in the Position Paper. This paper will be an important source of information and therefore an appropriate place to incorporate information on the penalty system.

We understand the ATO may impose 'failure to lodge' penalties if an SMSF fails to report by the required date. Consequently, we think it is imperative the ATO continues to state that during the transitional periods they will endeavour to assist people comply with the shift to more frequent event-based reporting but advisors need to be aware of the risks of delayed reporting.

Furthermore, it is essential that the penalty system is designed to deter trustees from delaying lodgement of their TBAR in order to rectify an inadvertent breach of the TBC.

Reversionary pensions

We note the ATO Position Paper also needs to clarify the reporting position regarding reversionary income streams. Both scenarios involving reversionary income streams state the reporting needs to include the commencement date and value of the reversionary income stream no later than 28 days after the end of the quarter in which the individual becomes entitled to the income stream. In these scenarios the ATO doesn't state the impact of the 12 month delay in reporting of the TBAR for reversionary income streams. This needs to be incorporated into the scenarios as to include reporting of the income stream 12 months and 28 days after the individual becomes entitled to the income stream.

If you have any questions about our submission please do not hesitate in contacting us.

Yours sincerely,

John Maroney
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SMSF Association