The Association of Superannuation Funds of Australia Limited
ABN 29 002 786 290
ASFA Secretariat
PO Box 1485, Sydney NSW 2001
p: 02 9264 9300 (1800 812 798 outside Sydney)
f: 02 9264 8824
w: www.superannuation.asn.au

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Penny Dally
Australian Taxation Office

Email: penny.dally@ato.gov.au

Dear Ms. Dally,

RE: Draft Taxation Ruling TR 2013/D7 – Income Tax: Apportionment of expenses incurred by a superannuation entity only partly in gaining its assessable income

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the request for comments on draft Taxation Ruling TR 2013/D7, which deals with the apportionment of expenses by superannuation entities.

We note the intent is for this ruling to replace the content in Taxation Ruling TR 93/17 to the extent that TR 93/17 deals with apportionment.

ASFA, whilst supportive of the proposal to update TR 93/17, is concerned with the prospect that the content of TR 93/17 is to be spread across two rulings and that, rather than being reviewed as a whole, two review processes will be undertaken.

About ASFA

ASFA is a non-profit, non-politically aligned national organisation. We are the peak policy and research body for the superannuation sector. Our mandate is to develop and advocate policy in the best long-term interest of fund members. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90% of the 12 million Australians with superannuation.

General comments

In early 2013 the ATO sought comments on the scope of the proposed content for a replacement Ruling for TR 93/17. In our response ASFA strongly supported the proposal to expand the content of TR 93/17 and provide examples as to how the law applies. We noted that there was likely to be great interest in the replacement Ruling across all of the superannuation industry and requested that the replacement Ruling be issued first as a Draft Ruling and that sufficient time were provided for interested parties to make comments on the Draft. We further requested that the ATO commit to taking into consideration all comments received during the consultation process prior to the finalisation of the Ruling.

We are concerned that, rather than issuing a comprehensive revision of TR 93/17, a piecemeal approach has been adopted to the rewrite. As we understand it, a draft ruling on the remaining

content of TR 93/17 is planned for release in March 2014. Such an approach seems premised on an assumption that there is no interaction between or cross-referencing of the various parts of TR 93/17. Whilst that may appear to be the case, it may not continue to be so as the comprehensive reanalysis of the law progresses.

ASFA's strong preference is that the outcome of this consultation process be incorporated into the proposed March 2014 consultative process, thus providing the industry with the opportunity to comment on a comprehensive rewrite of TR 93/17.

A further issue is that, by targeting only one aspect of that ruling (apportionment of expenditure which is incurred partly in producing assessable income and partly in gaining exempt income), tax practitioners will be required to consult two rulings, one on deductibility and one on apportionment (i.e. the extent of deductibility), on what is basically a single topic: deductibility of expenses. Such an outcome is not conducive to efficient interpretation and administration of legal obligations.

In summary, ASFA's preferred position is that TR 93/17 be replaced by a single comprehensive ruling focused on section 8-1 of the *Income Tax Assessment Act 1997* and which looks at specific deduction provisions only to the extent necessary to clarify whether or not an item is deductible under a specific provision rather than under section 8-1.

> **Recommendation**
> ASFA strongly recommends that the outcome of this consultation process be incorporated into the proposed March 2014 consultative process, thus providing the industry with the opportunity to comment on a comprehensive rewrite of TR 93/17

Specific comments on TR 2013/D7

ASFA is generally in agreement with the approach adopted by the draft ruling, noting that there is minimal deviation from the position set out in TR 93/17 and that some useful examples have been included.

The broad approach of the ruling appears to be that, while various indifferent expense apportionment methodologies are permitted, the methodology adopted should bear some relationship to the activities being undertaken. For example, an appropriate methodology for investment expenses should reflect that a part of the indifferent expense may relate to the gaining of non-assessable investment income. However, where the indifferent expense cannot be attributable to a specific activity, such as the earning of investment income or the receipt of contributions, then the 'income ratio method' may be used. ASFA supports this general approach.

Cost of Compliance

ASFA is concerned that the application of the income ratio method potentially may make the calculation of the pension portion of costs more complex with, in most cases, little difference in outcome. For superannuation funds with subdivisions or investment pools, it could be construed that deductions need to be determined on a division/pool by division/pool basis, rather than being able to group expenses. Additionally, depending on the granularity with which investment returns are calculated on an after-tax basis, there may be a significant amount of work required in accurately apportioning expenses. Given this, it is essential that funds be permitted to choose another method that is simpler, provided it delivers a fair and reasonable apportionment of expenses, rather than being required to use the method specified in the 'relevant' example. In this regard, we refer to paragraph 41, which is discussed later in this submission.

Distinction between contribution types

We note that in the various examples a distinction is made between assessable and non-assessable contributions, with each being listed separately for inclusion. ASFA considers that this

approach may cause confusion and lead the reader to an assumption that there may be certain circumstances where indifferent expenses are to be apportioned based on the ratio of assessable to non-assessable contributions.

Recommendation
ASFA recommends that for clarity and consistency with subsection 295-95(1) of the *Income Tax Assessment Act 1997*:

The interpretation section is amended to include the term **all contributions** and that the term references section 295-95(1) of the Act; and

The term **all contributions** be used in the examples in place of references to assessable and non-assessable contributions.

Example 5
Example 5 deals with the situation where a merger of funds late in the financial year results in what appears to be an anomalous situation: a significant increase in the deductible portion of an indifferent expense.

ASFA considers that the inclusion of this example introduces an unnecessary degree of uncertainty to the operation of the law. Effectively the ruling says that if the calculation you make gives you a 'generous' result then you should modify the methodology to something that the Commissioner would consider fairer and more reasonable.

In part, this problem arises from the treatment of fund mergers as a rollover of benefits, rather than the transfer of assets between funds.

Recommendation
ASFA recommends that a new opening paragraph to Example 5 be included that explains the purpose of the example is to demonstrate that situations may occur where a standard methodology may not be appropriate and that an alternative methodology may need to be adopted.

Use of other appropriate methods
The concluding paragraph to example 5 states:

41. Alternatively, the fund may choose another method of apportionment that gives a fair and reasonable assessment in the circumstances of the extent to which those expenses relate to gaining or producing the superannuation entity's assessable income.

ASFA considers that the concept expressed in this paragraph is the basic principle that should apply to apportionment. That is, the method to be adopted is that which gives a fair and reasonable assessment in the circumstances of the extent to which those expenses relate to gaining or producing the superannuation entity's assessable income. There will be a range of circumstances where, for specific indifferent expenses, an apportionment method other than the two set out in this ruling will be obviously appropriate and provide a fair and reasonable outcome. It should be made clearer within the ruling that any apportionment method that produces a fair and reasonable result may be used and that the purpose of the ruling is to provide 'safe harbour' rules and guidance on how to determine which rule is the more appropriate to apply.

Recommendation
ASFA strongly recommends that:

- The ruling clearly sets out that the basic principle on apportionment is that 'the method to be adopted is that which gives a fair and reasonable assessment in the

circumstances of the extent to which those expenses relate to gaining or producing the superannuation entity's assessable income'.

- The basic principle be clearly expressed earlier in the ruling (perhaps after, or as part of, paragraph 9); and
- It is made clearer that the two methods set out in the ruling and the examples provide a 'safe harbour' for trustees but that other method may be available to them to use (provided fair and reasonable).

* * * *

I trust that the information contained in this submission is of value.

If you have any queries or comments regarding the contents of our submission, please contact ASFA's Principal Policy Adviser, Robert Hodge, on (02) 8079 0806 or by email rhodge@superannuation.asn.au.

Yours sincerely

Fiona Galbraith
Director, Policy