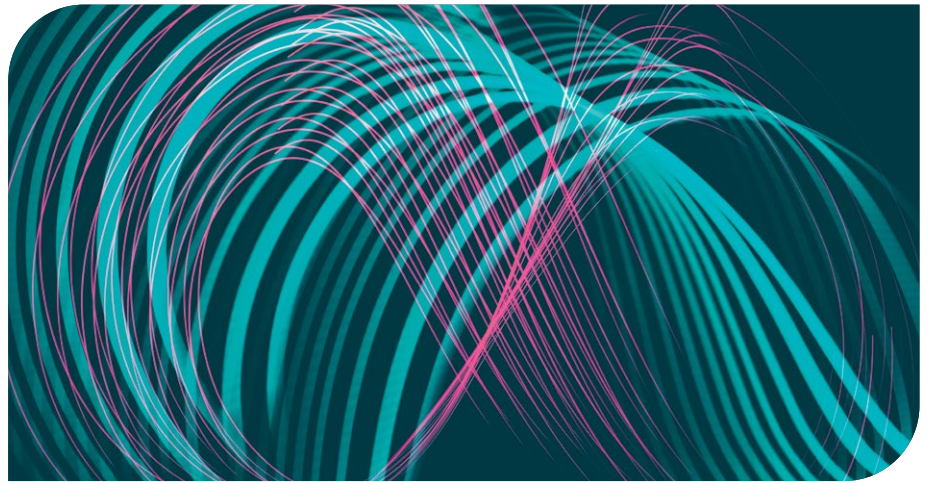


Superannuation Solutions

Edition 18



Welcome

Welcome to the latest edition of our Superannuation Solutions Newsletter.

In this edition we discuss compulsory contribution changes, an exposure draft of NALE legislation, the results of the 2023 super performance test and SuperStream rollover dates.

We hope you find this newsletter informative. Should you have any questions in relation to how these changes may impact you, please contact one of our SMSF Specialists.

Important Dates

28 October 2023

Lodge any transfer balance account transactions between 1 July 2022 and 30 September 2023 not previously lodged.

28 October 2023

Pay compulsory super contributions for the quarter ended 30 September 2023.

28 November 2023

Lodge super guarantee charge statement and pay super guarantee charge if compulsory contributions not made for the quarter ended 30 September 2023.

Compulsory super contribution rate increases to 11%

Clients should note that the compulsory super guarantee contribution rate has increased from 10.5% to 11%. The increased rate applies to salary and wages paid on or after 1 July 2023.

Planned future increases in the super guarantee rate are:

From 1 July 2024 11.5%

From 1 July 2025 12%

Clients should also remember that the \$450 per month threshold under which super guarantee contributions did not have to be made was abolished from **1 July 2022**. Contributions must be made for all employees aged over 18, regardless of how much they are paid.

There is still an exemption for employees under 18 who work less than 30 hours in a week, but employers must monitor the number of hours worked by these employees. Contributions must be made for all employees under 18 if they work more than 30 hours in a week, regardless of how much they are paid.



Exposure draft of NALE legislation released

In the 2023 Budget the Federal Government announced how it intended to solve the problem of non-arm's length general expenses in super funds. An exposure draft of relevant legislation has been released for comment, and it seems likely that it will be enacted. But the proposed solution leaves many issues unresolved and imposes additional responsibilities on fund trustees to avoid ATO action.

Background

For many years the income tax law has contained a provision which taxes at a penalty rate of 45% any income of a super fund which is artificially inflated above an arm's length amount (non-arm's length income, or NALI). This is intended to prevent income from being diverted into the tax-advantaged super environment. Readers may be aware that the law was amended with effect from 1 July 2018 so that where a super fund incurs an expense (of either a capital or revenue nature) less than an arm's length amount (non-arm's length expenses or NALE), any income connected with that expense is also treated as non-arm's length income and taxed at the penalty rate.

The Problem of General Expenses

The NALE provisions can potentially apply to any expenses incurred by super funds. The issue of "general expenses" is of particular concern. A number of super fund expenses such as accounting, audit and actuarial fees potentially relate to all income derived by a fund. In a situation where, for example, the fund is provided with free accounting services by a firm related to a member, the non-arm's length nature of this relatively minor expenditure could result in the entire income of the fund being treated as non-arm's length income (NALI).

The NALE debate

There continues to be a long-running debate between the Federal Government and professional bodies about the problems associated with the 2018 NALE provisions and whether there is a need for them at all. In February this year seven tax and accounting bodies including CA ANZ, the Tax Institute and the SMSF Association released a *Joint Submission to Treasury on NALE Rules for Superannuation*, arguing that the NALE amendments created more problems than they solved, and that the potential tax avoidance issues could be dealt with by existing provisions of the law.

The Federal Government seems to be intent on implementing the NALE provisions in some form or another, but intends to limit the potential amount of fund income that could be NALI because of a general NALE expense.

The proposed amendments

The amendment offered in the exposure draft, in line with the earlier Budget announcement, proposes that the NALE rules will only apply to funds with 6 or fewer members (that is, SMSFs and small APRA funds). Large APRA funds (mainly retail funds, industry funds and tax-exempt public sector funds) will be completely exempted from the NALE rules for both general and specific expenses, but will still be subject to the original NALI provisions. For funds with 6 or fewer members, a distinction will be made between expenses that do not relate to any particular asset or assets of the fund (general expenses) and expenses that relate to a particular

asset. Where a NALE general expense has been incurred, the maximum amount of fund income that can be treated as NALI will be twice the difference between the amount that would have been incurred as an arm's length expense and the amount that was actually incurred by the fund, but this will be capped at a maximum of the fund's taxable income not including assessable contributions.

The problems

The proposed "twice the difference" cap will only apply to general expenses, and not to NALE expenses incurred in relation to specific assets. Where, for example, a property is acquired by a fund for less than its market value, all the rental income and any capital gain on ultimate disposal will be regarded as NALI. An even more severe example would be that of a tradie member of a super fund who gives his labour for free to make repairs to a property owned by the fund. As the fund was not charged an arm's-length fee for the member's labour, this is an example of a NALE expense which relates to a specific asset. All income arising from the property concerned, and any ultimate capital gain, will be regarded as NALI and subject to tax at penalty rates without the restriction of the "twice the difference cap", even if the member's work on the property was relatively minor.

It should also be noted that where the income from a long-term asset has been tainted as NALI, there is currently no provision to allow this to be rectified. In the example above of a property, there is nothing the fund can do to reverse the problem of a non-arm's length expense.

A further problem is that the proposed "twice the difference" cap will only apply to general expenses of a revenue nature, and not to general expenses of a capital nature. One example of a general expense which might be of a capital nature is the cost of updating the fund's trust deed. It is possible that if a fund does not pay an arm's length fee for updating its trust deed, the entire income of the fund in that year could be rendered NALI and taxed at 45%.

The decision to exempt large funds from the NALE rules means that the rules are clearly focused on SMSFs. This seems hard to justify, and the joint accounting bodies have argued that this will create a two-tiered superannuation sector with a tax differential between the tiers.

The operation of the NALI and NALE provisions also raises the issue of the need to document that expenses incurred by the fund were arm's length. There are two external parties who might call for such documentation: the fund's auditor and the ATO.

The auditor of a super fund is required to report on two aspects of the fund's operation each year. The first (Part A) is a financial audit of the fund, with an expression of opinion as to whether the financial report presents fairly the financial position of the fund at year end and the results of its operations for the year. The second (Part B) is a compliance audit, with an expression of opinion as to whether the fund complied with the SIS regulations. The question of whether some part of a fund's income is NALI, and therefore subject to a higher rate of tax, is not a breach of SIS compliance. Instead, it is a matter of whether the provision for income tax in the fund's financial statements is materially correct. The fund's auditor is not required to (but may choose to) report to the ATO that a fund has not recognised the effect of NALI in its tax provision.

Further, the auditor will probably assess whether it is reasonable to investigate NALI issues on the basis of materiality. The auditor may choose to take no action where there is only a low risk that the trustees have not detected or not disclosed a significant NALI issue.

Even so, it would be wise to obtain and keep documentation supporting the arm's length nature of fund expenses in case the ATO wishes to review the fund's operations.

In terms of application, these latest amendments are intended to operate in relation to NALE general expenses in the 2023-24 and later tax years. In relation to the 2018-19 to 2022-23 years, funds will need to rely on the ATO's earlier statements that it will not devote compliance resources to investigating NALE general expenses.

Please contact your Nexia advisor if you have any questions in relation to NALI or NALE and your super fund.



Results of the 2023 super performance test

The Australian Prudential Regulation Authority (APRA) has released the results of the 2023 superannuation performance test. This annual test first took place in 2021 as part of a raft of reforms introduced by the previous Federal Government to improve returns from superannuation and to make the investment performance of funds more transparent.

For the first two years the performance test included only MySuper products. These are basic super products mostly used as default employer funds or by individuals who don't want any special features like investment choice in their fund.

In 2021 (the first year of the test) 13 MySuper products failed. After a number of products merged or closed, in 2022 (the second year of the test) one MySuper product failed for the first time and four failed for the second time. In the 2023 test no MySuper products failed for the first time, but one has failed for the third time.

The 2023 performance test was expanded to include trustee directed products, where the trustee has control over the design of the investment strategy of the product. Typically this also allows the fund member some element of investment choice. Of the 805 trustee directed products tested, 96 failed. APRA has pointed out that 75% of the failed trustee directed products are concentrated in products offered by just four trustees.

Trustees of products that failed to pass the benchmarks must notify their members of the test outcomes by 28 September 2023. Trustees cannot accept new members into products that have failed for two consecutive years.

Further details of the performance test is available from the APRA website at [APRA releases 2023 superannuation performance test results | APRA](#)

All SMSFs to use SuperStream for rollovers from 1 July 2023

SuperStream is a digital process designed to simplify and speed up the processing of employer contributions and rollovers by super funds. It requires that all participating super funds must have an electronic service address (ESA). All employer contributions are required to be processed by SuperStream, except where they are made to a related SMSF.

Although SMSFs have been required to process rollovers using SuperStream since 1 October 2021, the ATO provided temporary relief by allowing rollovers between SMSFs and from an SMSF to be processed outside SuperStream without incurring penalties. This concession recognised that the original pool of ESA providers who could process rollovers was limited.

Trustees should be aware that this temporary relief ended on 1 July 2023. From that date all rollovers to and from an SMSF must

be executed through SuperStream, requiring the fund to have an ESA from a provider who is rollover enabled. SMSF auditors will now be required to report any rollover not executed through SuperStream as a compliance breach.

Nexia provides this facility to all our client funds through our specialised super fund software platforms. Fund trustees who are not clients may be interested in the ATO's list of current ESA providers at [ATO ESA providers](#).

Most people are not familiar with the details of how SuperStream operates for rollovers and the timing requirements. Please contact your Nexia advisor if you plan to initiate a rollover into or out of your SMSF, so the necessary steps can be planned well in advance of the rollover happening.



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With the wealth of knowledge that comes with 30 years of excellence, a global network, and connections like Bursars' Associations, Independent Schools Associations, the Department of Education, Employment, and Workplace Relations, as well as consulting and bank executives — you can focus on setting 'new' goals instead of worrying about 'how' to reach your current ones.

We take pride in being responsive, progressive, and proactive in identifying and implementing the solution to your success.

Contact us

Learn how Nexia Australia can help set you and your organisation up for success. Contact your local Nexia Advisor below to get started.

Australia

Adelaide Office

Level 3, 153 Flinders Street Adelaide SA 5000
GPO Box 2163, Adelaide SA 5001
p +61 8 8139 1111, f +61 8 8139 1100
www.nexiaem.com.au

Brisbane Office

Level 28, 10 Eagle Street Brisbane QLD 4000
GPO Box 1189 Brisbane QLD 4001
p +61 7 3229 2022, f +61 7 3229 3277
www.nexia.com.au

Canberra Office

Level 5, 17 Moore Street, Canberra ACT 2601
GPO Box 500, Canberra ACT 2601
p +61 2 6279 5400, f +61 2 6279 5444
www.nexia.com.au

Darwin Office

Level 2, 80 Mitchell Street Darwin NT 0800
GPO Box 3770, Darwin NT 0801
p +61 8 8981 5585, f +61 8 8981 5586
www.nexiaemnt.com.au

Melbourne Office

Level 35, 600 Bourke Street
Melbourne VIC 3000
p +61 3 8613 8888, f +61 3 8613 8800
www.nexia.com.au

Perth Office

Level 3, 88 William Street, Perth WA 6000
GPO Box 2570, Perth WA 6001
p +61 8 9463 2463, f +61 8 9463 2499
www.nexia.com.au

Sydney Office

Level 22, 2 Market Street, Sydney NSW 2000
PO Box Q776, QVB NSW 1230
p +61 2 9251 4600, f +61 2 9251 7138
www.nexia.com.au

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