EXCESS CONTRIBUTIONS TAX – WHERE ARE WE NOW?

The Government announced a number of changes in relation to excess contributions tax ("ECT") during 2011.

Before considering the effect of these announcements it might first be helpful to describe the ECT in general terms.

Limiting the superannuation concessions

The Government has, for a long time, imposed limits on the availability of superannuation tax concessions. Prior to 2007, it sought to do this through imposing age based deduction limits for contributions and restrictions on the amount of benefits that could be received concessionally (known as the "reasonable benefits limits"). Since then, the restrictions have focussed on the amount of contributions that can be made to superannuation by or in respect of a member.

The tax on excess contributions

Under the current arrangements, contributions are divided into two types:

- *Concessional* - essentially employer contributions and deductible member contributions; and
- *Non-concessional* – essentially non-deductible member contributions.

Each type of contribution has a dollar cap that applies in each tax year. If these caps are exceeded then additional tax is payable by the member.

Note also that a superannuation fund may not accept non-concessional contributions that are, in themselves, in excess of the contribution caps. Therefore, the acceptance of an excessive non-concessional contribution by a fund would raise compliance issues for the fund (in addition to the ECT issue for the member).

The additional tax is of such amount as to result in the excess contribution being taxed at 46.5%.

Members must withdraw non-concessional ECT from their superannuation fund. For concessional ECT they can either pay the tax themselves or withdraw the tax payment from their superannuation fund.

The contribution caps

The contribution caps have undergone changes over time and the caps for the 2011-12 tax year (which are the same as those that applied for the 2009-10 and 2010-11 tax years) are used below.

Non-concessional contributions

The non-concessional cap is currently $150,000. However, for members under age 65 the non-concessional caps for the following 2 years can be brought forward to give a single year $450,000 cap. No election by the member is actually involved. If the non-concessional cap is exceeded then the "bring forward" applies automatically.

It should also be noted that amounts in excess of the concessional contributions cap count towards the non-concessional cap - leading to the possibility of a 93% tax rate in situations where very large excess contributions are made.

Concessional contributions

The concessional cap is generally $25,000. However, a higher cap of $50,000 applies until 30 June 2012 for members who are over age 50. The Government has announced that from 1 July 2012 the higher cap will continue for members over age 50 with superannuation account balances of less than $500,000.

The concessional cap is subject to indexation based on increases in the consumer price index. However, the indexation does not apply until the increase exceeds $5,000. For a number of reasons, it is unlikely that the concessional cap will increase before 1 July 2014, at which time it will become $30,000 (with the consequence that the non-concessional cap will become $180,000).

The problems

There are a number of issues that have arisen with the excess contributions system. These include:

- The bringing forward of the 3 year cap as soon as the non-concessional cap is exceeded by even $1 in a year.
- The punitive nature of the 93% tax rate.
- The inadvertent breaching of the caps for a number of reasons such as:
  - contributions for one tax year being received in the following tax year,
  - the halving of the caps from their original levels,
  - co-ordination issues for taxpayers with multiple employers,
- The inflexibility of the ATO's approach to disregard excess contributions or reallocate them to another tax year.

Proposed relief for excess concessional contributions

In the 2011 Federal Budget the Government announced that the severity of the ECT regime would be mitigated slightly by permitting a one-off refund of excess concessional contributions to a member.

This concession will only apply to the first breach of the concessional contribution cap after 1 July 2011 and only where the excess contribution amount is $10,000 or less. However, if the member does not accept the first refund "offer" from the ATO they will no longer be eligible for a refund in a later year.

The exposure draft legislation released by Treasury proposes that the fund will refund the excess contribution to the ATO rather than direct to the member. This amount will then constitute a refundable tax credit against the member's overall tax liability. As a result, the refunded amount will, effectively, be taxable to the member at his or her marginal tax rate. A tax offset will apply for the contribution tax paid in the fund.

The proposal was expressed to take effect from 1 July 2011.

Prohibition of contribution "non-acceptance" clauses

In response to the ECT problems mentioned above, some SMSF trust deeds have included clauses that purported to prevent the trustee from accepting contributions that would be excessive having regard to the overall position of the member. Any amount not accepted as a contribution would then be held on trust for the contributor outside of the fund.

The effectiveness of such clauses has been questioned but the Government will remove any doubt in this regard by amending the law to deem such payments to be contributions accepted by the trustee of the SMSF despite the inclusion of such a clause in the trust deed. No effective date for this change was indicated in the announcement. However, given the anti-avoidance flavour of the change it is possible that it will be given retrospective operation.

6 January 2012.