

QAR final report and additional 15% super tax

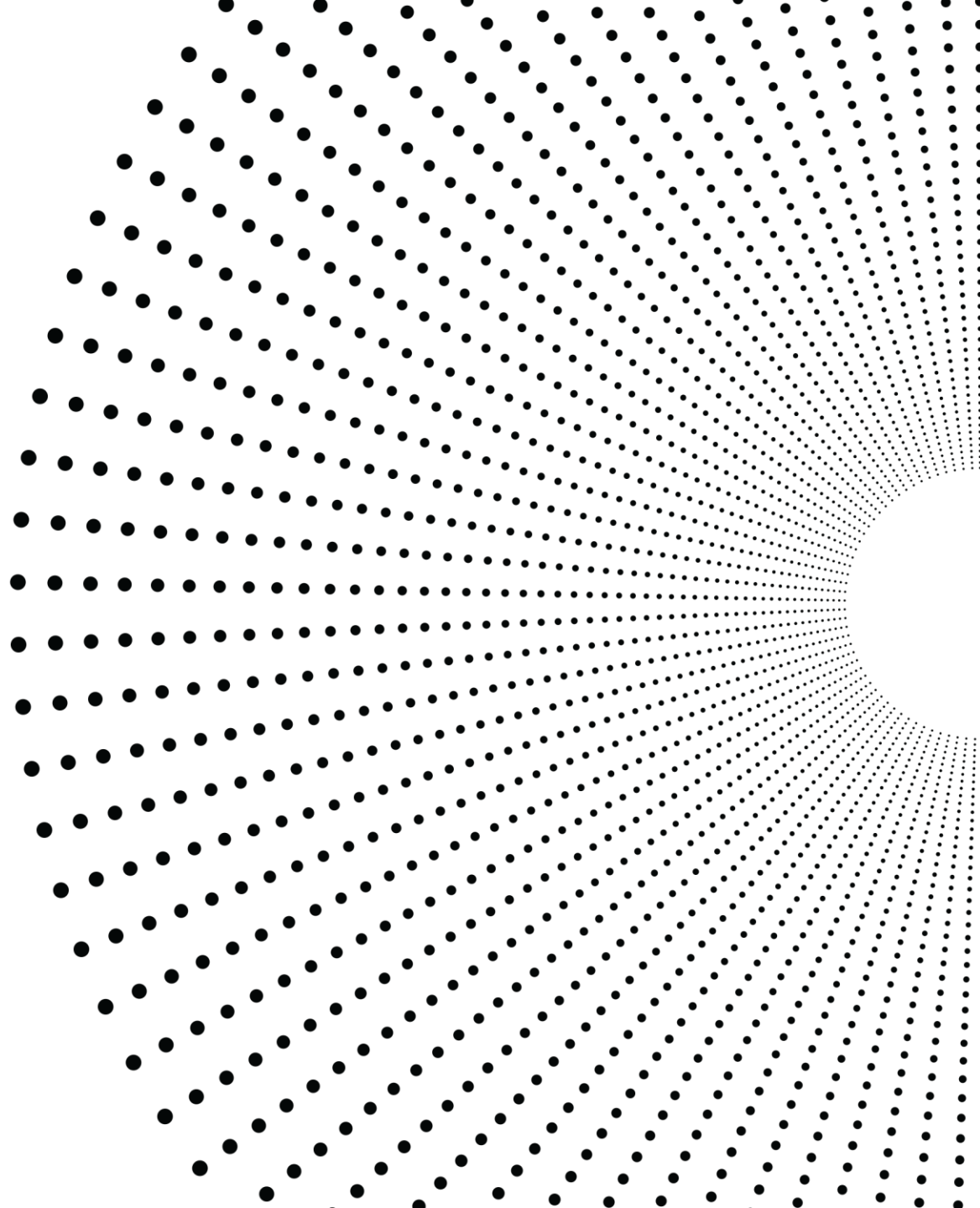
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May 2023

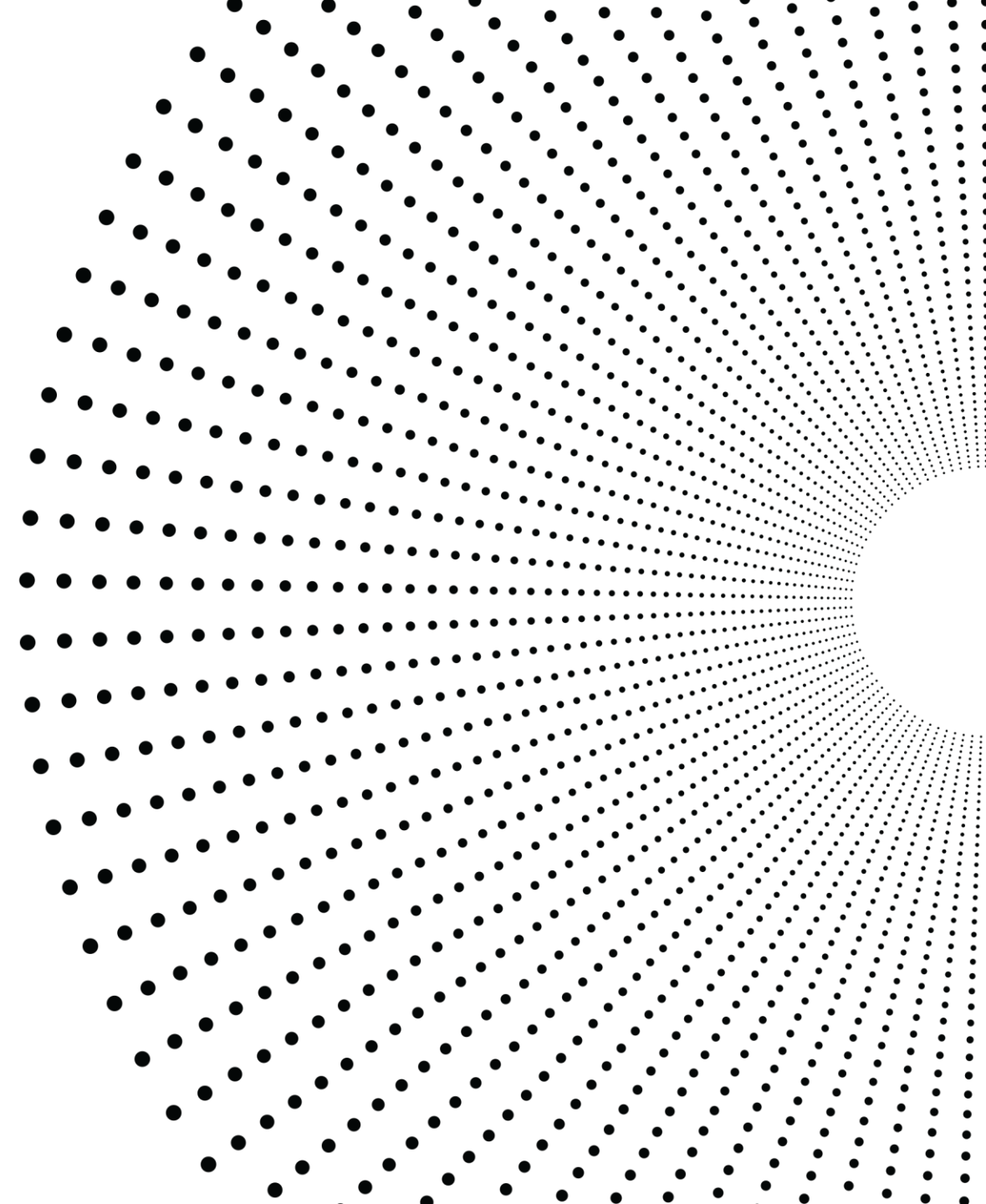


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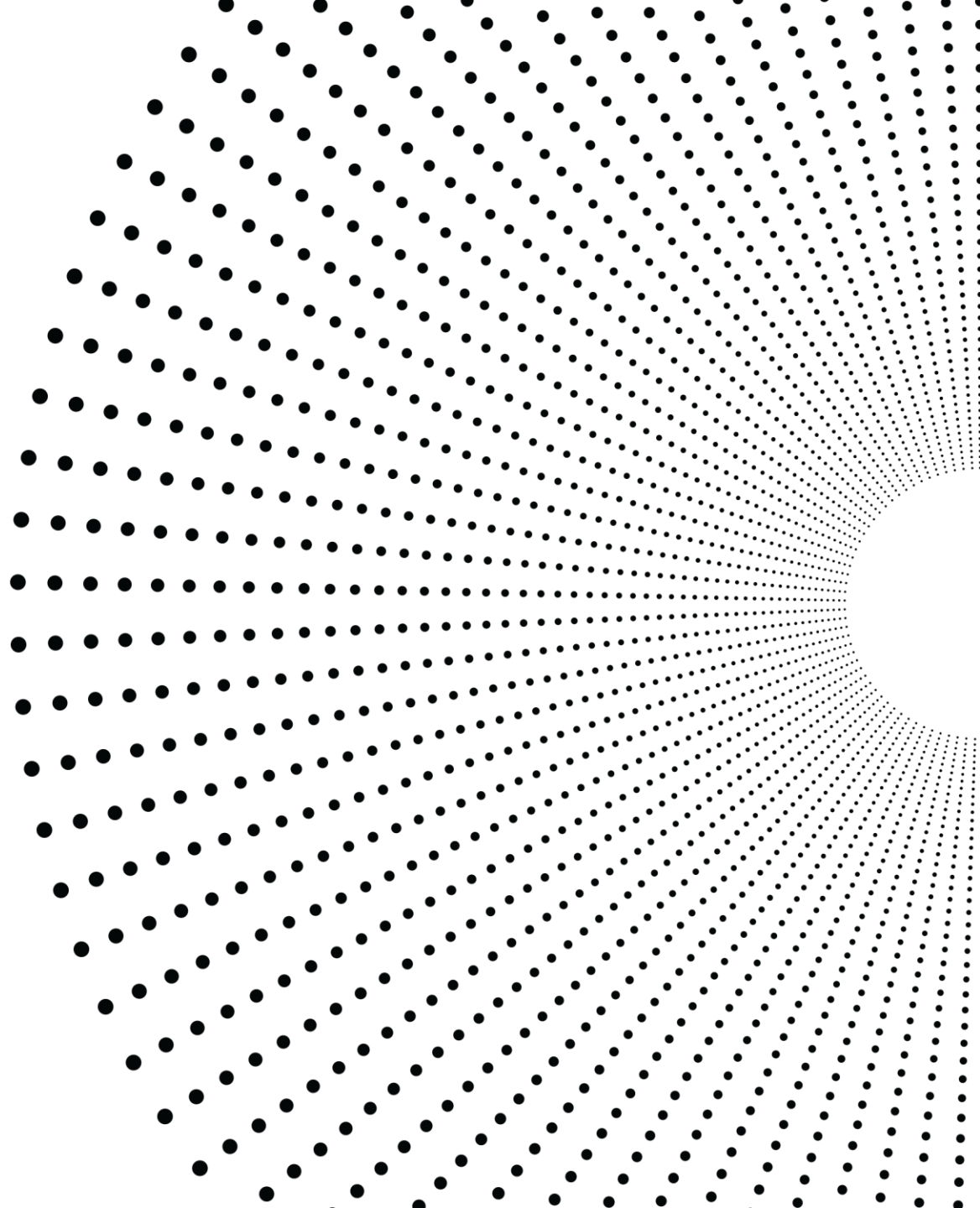
Agenda

| | | |
|----|-----------------------------------|-------|
| 01 | QAR Final Report | David |
| | Additional 15% super tax | |
| 02 | TSB explanation | Will |
| | Additional 15% super tax examples | David |



01

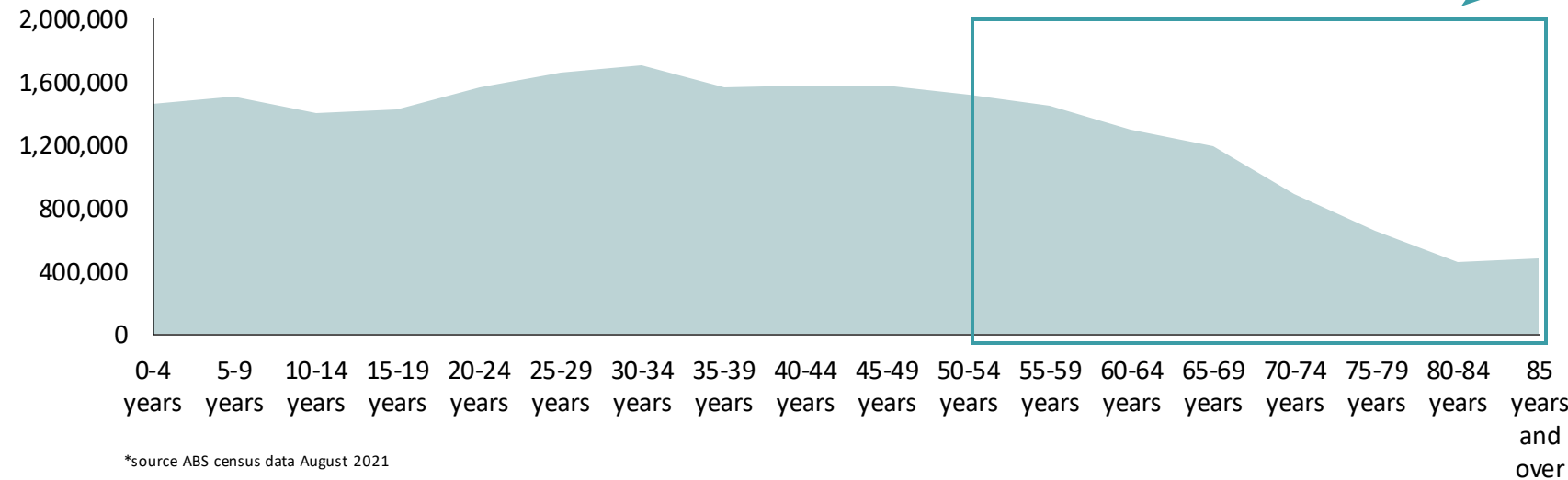
Quality of Advice Review



01 – Quality of Advice Review

The issue to be resolved...

Population August 2021 – 25.4 million*



7.95 million age 50+ (31%)

ASIC FAR as at 2 Feb 2023:
No. of advisers = 16,413 (down from peak of >28,500 in late 2018, and decreasing...)
Estimate ~15,000 active advisers
If 100 clients per adviser, then:
• capacity to advise ~1.5 million clients

Conclusion:
1. Advice industry supply cannot meet potential advice demand
2. Policy change needed...

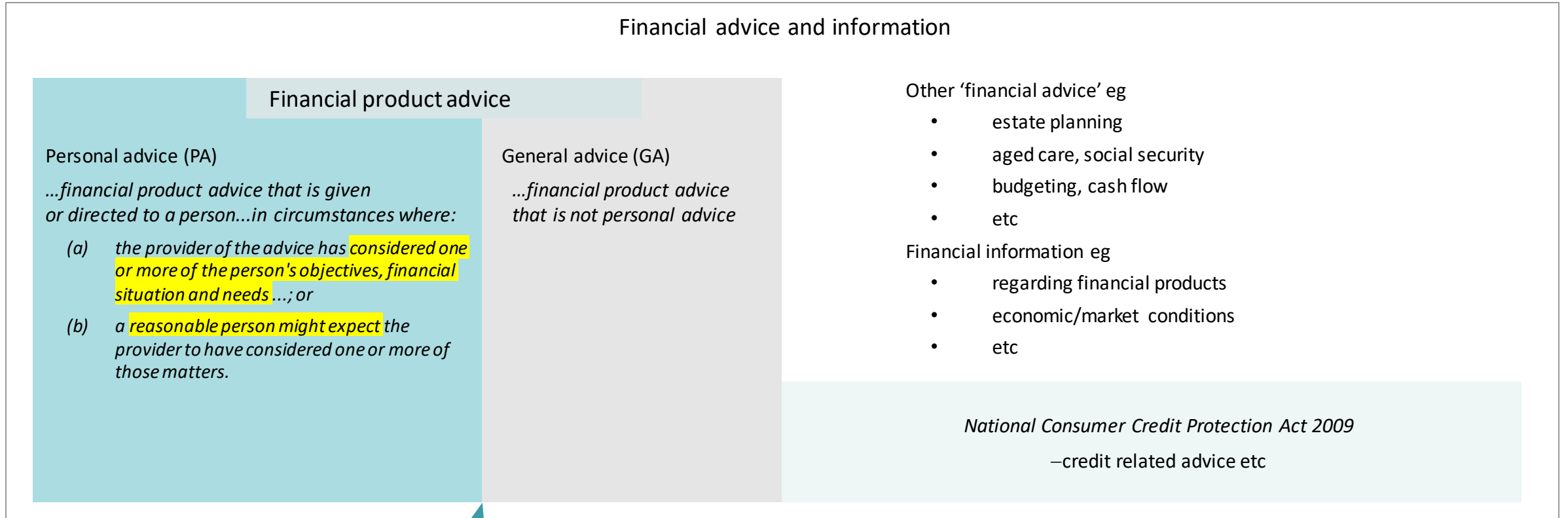
Aim of QAR:

'...how the regulatory framework could better enable the provision of high quality, accessible and affordable financial advice for retail investors' – QAR Terms of Reference

- QAR Final Report released 8 February 2023

01 – Quality of Advice Review

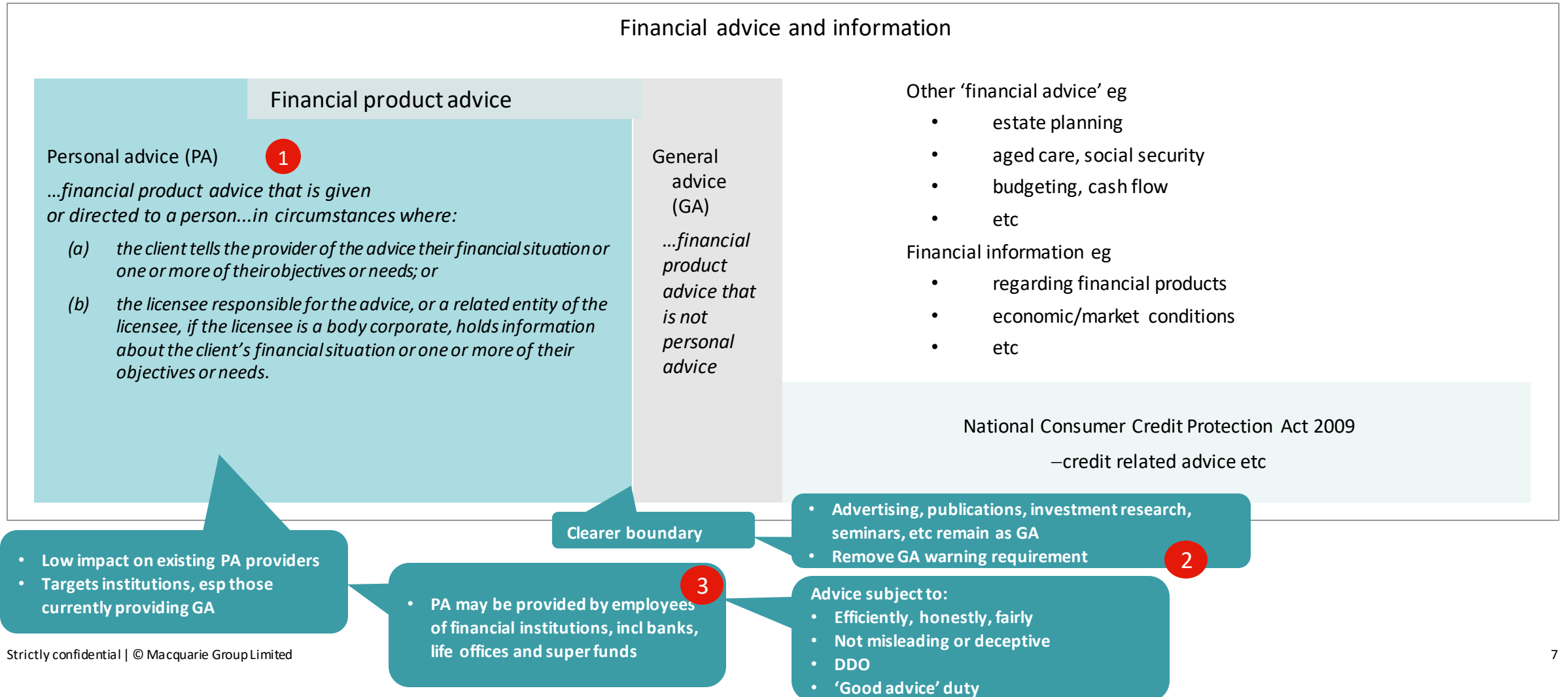
Definition of ‘personal advice’ – current position



Confusion and litigation over this boundary

01 – Quality of Advice Review

Recommendations 1, 2 and 3



01 – Quality of Advice Review

Recommendations 4 and 5

| Current position – best interests duty (BID) | Proposed position |
|---|--|
| <p>S 961B(1):</p> <p><i>Must act in the best interests of the client in relation to the advice.</i></p> <p>S 961B(2) safe harbour steps:</p> <ol style="list-style-type: none">1. Identify the client's needs and objectives2. Identify the subject matter of advice sought by the client3. Make reasonable enquiries to obtain complete and accurate information4. Assess whether the adviser has the expertise to provide the advice5. Research products that might meet the needs and objectives of the client6. Base all judgements on the client's needs and objectives7. Take any other step that would reasonably be regarded as being in the best interests of the client | <p>'Good advice' duty – all personal advice providers 4</p> <p><i>A person who provides personal advice should be required to provide 'good advice'.</i></p> <p><i>'Good advice' is advice that would be reasonably likely to benefit the client, having regard to the information that is available to the provider at the time the advice is provided.</i></p> |
| | <p>Best interests duty – relevant providers 5</p> <p><i>The new best interests duty would be a true fiduciary duty that reflects the general law and will not include a safe harbour.</i></p> |

Financial Adviser Code of Ethics

Standard 2:

You must act with integrity and in the best interests of each of your clients

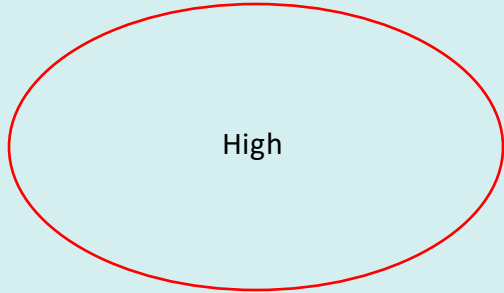
01 – Quality of Advice Review

Possible impact of proposals

| Key proposals | Relevant provider impact | Product provider (AFSL) impact |
|----------------------------------|--------------------------|--------------------------------|
| 1. Broaden PA | Low | High |
| 2. Remove GA warning requirement | Very low | |
| 3. PA for fee/commission etc | Low | |
| 4. Good advice duty | Moderate | |
| 5. Revised statutory BID for RPs | | |

Existing PA providers, servicing ~1.5m clients

PA which is 'good advice' to a much wider audience



16 million Australians have superannuation

Broadly maintain the status quo, but improve delivery of an already high quality service

| Key proposals | Relevant provider impact | Super fund (AFSL) impact |
|--|--------------------------|--------------------------|
| 6. Superannuation advice and charging powers | Low-moderate | Moderate |
| 7. Deduction of adviser fees from superannuation | | |

Both recommendations are regarding member's interest in the super fund

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Possible impact of proposals

| Key proposals | Relevant provider impact | Product provider (AFSL) impact |
|---|--------------------------|--------------------------------|
| 8. Ongoing fee arrangements and consent requirements <ul style="list-style-type: none">• Prescribed single consent form | Medium-high | Currently N/A |
| 9. Statement of advice requirement removed <ul style="list-style-type: none">• Complete records• Written advice on request | High | Currently N/A |
| 10. Financial Services Guides online | Low | Low |
| 11. Consent requirements for wholesale clients (QAC) | Low-moderate | Low |

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Possible impact of proposals

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|---|--------------------------|--------------------------------|
| 8. Ongoing fee arrangements and consent requirements <ul style="list-style-type: none"> • Prescribed single consent form | Medium-high | Currently N/A |
| 9. Statement of advice requirement removed <ul style="list-style-type: none"> • Complete records • Written advice on request | High | Currently N/A |
| 10. Financial Services Guides online | Low | Low |
| 11. Consent requirements for wholesale clients (QAC) | Low-moderate | Low |
| 12. DDO distribution and reporting requirements <ul style="list-style-type: none"> • Exemptions for RPs only • Reduce reporting for RPs | Low | Low |
| 13. Conflicted remuneration adjustments <ul style="list-style-type: none"> • Various tidy-ups | Low | Low |

Consider impact of more widely available 'simple' advice on existing RPs...

01 – Quality of Advice Review

Non-relevant provider advice vs relevant provider advice

| Non-relevant providers (product centric) | Relevant providers |
|--|---|
| <p>Banks:</p> <ul style="list-style-type: none">• basic banking products• credit products <hr/> <p>Fund managers:</p> <ul style="list-style-type: none">• managed funds <hr/> <p>Insurance companies:</p> <ul style="list-style-type: none">• death, TPD, trauma, IP <hr/> <p>Super funds:</p> <ul style="list-style-type: none">• current intra-fund advice• areas of advice:<ul style="list-style-type: none">– investment options– contribution caps and issues– death benefit nominations– insurance options– retirement income options <hr/> <p>Finfluencers ??</p> | <p>More complex scenarios e.g.</p> <ul style="list-style-type: none">• Aged care• Cash flow management / budget• Centrelink• complex debt structures• SMSF lending – non-recourse loan set up• diversified portfolios (e.g. multiple fund managers, blended stocks/managed funds, etc)• buy-out, equalisation insurance arrangements• business insurance – key persons, buy-sells, etc• choice of super funds:<ul style="list-style-type: none">– industry, public sector, MySuper, choice, SMSF, etc• SMSF and wrap super advice• family super planning – spouse balances, etc• estate planning – POAs, medical/guardianship, wills, super noms and estate, testamentary trusts, etc <p>Value in ongoing relationship</p> |

Free advice?

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Next steps

- Government response late May/early June
 - potentially implement in 3 phases
- ALRC (review of financial services legislation) to report by 30 Nov 2023

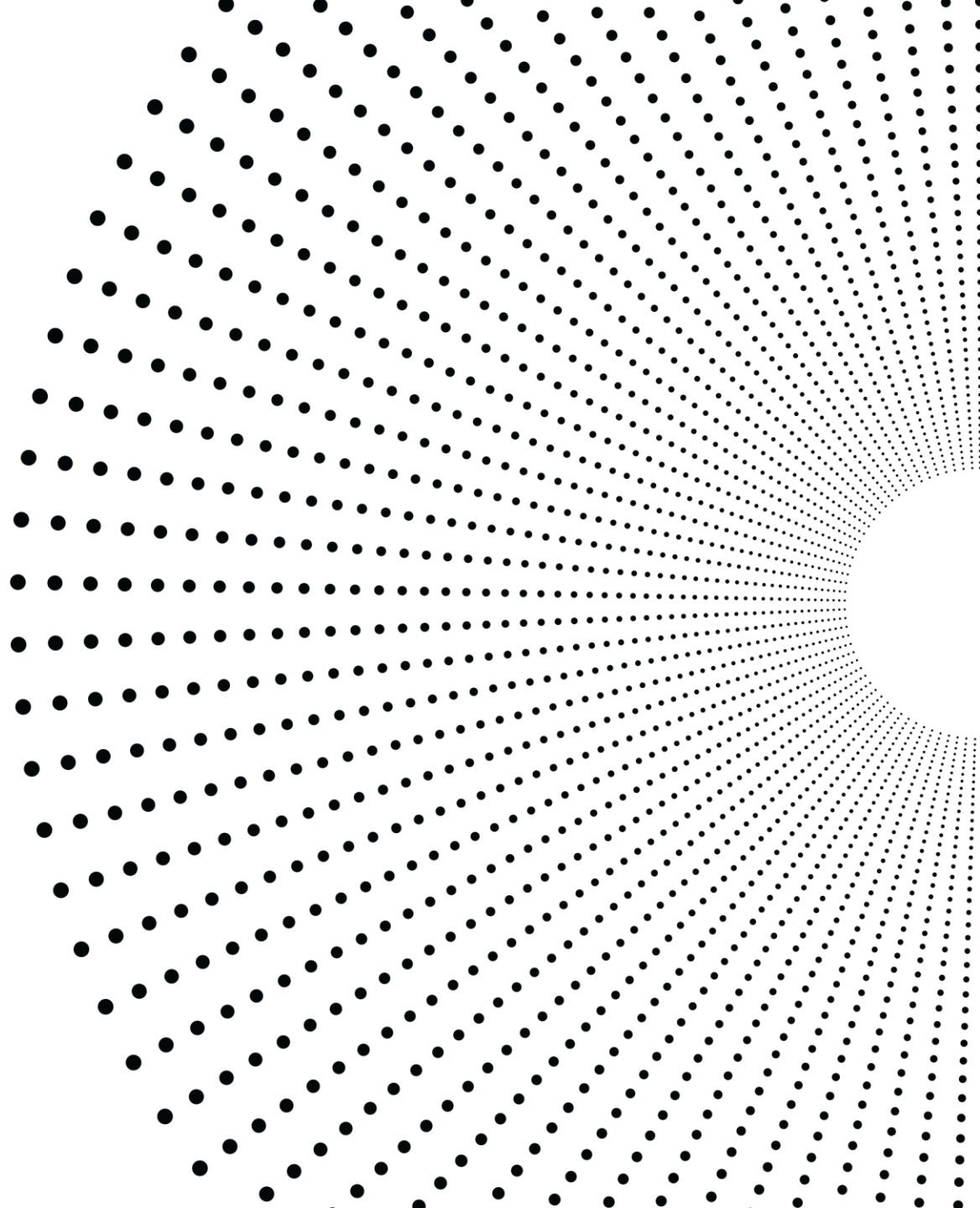
Polling question 1

Would you like to see the QAR Final Report recommendations implemented:

- a. In full (ie all recommendations)
- b. In part
- c. Not at all

02

Additional 15% super tax



02 – Additional 15% super tax

Proposed extra 15% super tax - announced 28 February 2023

Not indexed

- Earnings on super balances > \$3 million would be subject to extra 15% tax
 - 80,000 members affected (0.5%)
 - effective 2025-26, first assessment issued 2026-27 or later
- ATO to calculate tax using formula
 - intention to include DB interests
- Tax assessment sent to super fund member

Calculation method

Step 1 – Calculate the earnings for the year

$$Earnings = (TSB_{Current\ Financial\ Year} + Withdrawals - Net\ Contributions) - TSB_{Previous\ Financial\ Year}$$

Step 2 – Calculate the proportion of earnings that are assessed

$$Proportion\ of\ Earnings = \frac{TSB_{Current\ Financial\ Year} - \$3\ million}{TSB_{Current\ Financial\ Year}}$$

Step 3 – Calculate the tax

$$Tax\ Liability = 15\ per\ cent \times Earnings \times Proportion\ of\ Earnings$$

Reference: <https://treasury.gov.au/consultation/c2023-373973>

02 – Additional 15% super tax

Additional 15% super tax examples - Warren

Example – Warren (from Treasury factsheet)

- Warren is 52 with a total superannuation balance (TSB) of \$4 million at 30 June 2025. He makes no contributions or withdrawals. By 30 June 2026 his TSB has grown to \$4.5 million.

| Step | Warren |
|--|--|
| 1. Earnings = $(TSB_{\text{Current FY}} + W/\text{drawals} - \text{Conts}) - TSB_{\text{Previous FY}}$ | Earnings = $\$4.5\text{m} - \4m = \$500k |
| 2. Ppn of earnings = $(TSB_{\text{Current FY}} - \$3\text{ million}) / TSB_{\text{Current FY}}$ | Ppn = $(\$4.5\text{m} - \$3\text{m}) / \$4.5\text{m}$ = 33% |
| 3. Tax liability = $15\% \times \text{Earnings} \times \text{Ppn of earnings}$ | Tax liab = $15\% \times \$500\text{k} \times 33.3\%$ = \$24,750 |

Warren may:

- pay from personal financial resources, or
- send assessment on to one or more of his super funds

02 – Additional 15% super tax

Understanding total superannuation balance (TSB)

Accumulation phase interests

Includes – standard accum. accounts, TTRIS not in retirement phase (RP)*, deferred income streams not commenced and not in RP*

Valuing interest - general rule (laws may specify other method) = total benefits payable if account voluntarily closed (ie factor in costs of closing account eg CGT)

+

Retirement phase interests

Includes – account based income streams (eg ABPs, TRIS in RP*, market linked (aka TAPs)) and defined benefit pensions.

Valuing interest:

- General rule – Transfer Balance Cap (TBC) account value (not below zero)
- Modification – account based income streams – replace TBC value # for benefits payable if voluntarily closed

+

Rollovers in transit

Amount paid and yet to be received by other fund at 30 June

+

LRBA loans

New loans for SMSFs/SAFs from 1 July 2018 where:

- Certain condition of release met (ie age 65, retirement, terminal medical condition, permanent incapacity), and/or
- Lender is associate of fund

Excludes refinancing pre 1 July 2018 LRBA's if no increase to loan or change of security

Structured settlement/personal injury contributions

TSB modified to exclude these contributions

* Retirement phase means at least age 65 or satisfied either the retirement, terminal illness or permanent incapacity condition of release

Certain credits/debits retained in rare cases

Polling question 2

From your dealings with total super balance (TSB) and SMSFs, are the costs associated with closing an account (e.g. CGT on unrealised gains) factored into the reported value?

- a. All the time
- b. Sometimes, it depends on the accountant/administrator
- c. Never
- d. Don't know

02 – Additional 15% super tax

Policy development – technical considerations

How will 'withdrawals' be defined:

- Treatment of some payments (eg release due to excess contributions or Div 293)

Will the meaning of 'contributions' be modified:

- Include insurance proceeds?
- Include death benefit taken as pension?

Defined benefit schemes:

- Impact of increase in assessed value – move from accum. and pension
- Should there be a reducing value for annuity style inc. streams?

LRBAs

- Is increase to TSB for post 1 July 2018 arrangements appropriate (effectively double counts loan)?

Reserves

- Should reserves, not factored into income streams, be incorporated into TSB?

02 – Additional 15% super tax

Additional 15% super tax examples

Example – Carlos (adapted from Treasury CP)

- Carlos' SMSF has a superannuation balance of \$9 million on 30 June 2025, which grows to \$10.15 million on 30 June 2026. He makes no draw downs and no additional contributions to the fund.
- Carlos is 69 and retired. His SMSF has a superannuation balance of \$9 million on 30 June 2025, which grows to \$10 million on 30 June 2026. He draws down \$150,000 during the year and makes no additional contributions to the fund.

| Step | Carlos | Carlos (withdrawal) |
|--|--|--|
| 1. Earnings = $(TSB_{\text{Current FY}} + W/\text{drawals} - \text{Conts}) - TSB_{\text{Previous FY}}$ | Earnings = $\$10.15\text{m} - \9m = \$1.15m | Earnings = $(\$10\text{m} + 150\text{k}) - \9m = \$1.15m |
| 2. Ppn of earnings = $(TSB_{\text{Current FY}} - \$3\text{ million}) / TSB_{\text{Current FY}}$ | Ppn = $(\$10.15\text{m} - \$3\text{m}) / \$10.15\text{m}$ = 70.4% | Ppn = $(\$10 - \$3\text{m}) / \$10\text{m}$ = 70% |
| 3. Tax liability = 15% x Earnings x Ppn of earnings | Tax liab = $15\% \times \$1.15\text{m} \times 70.4\%$ = \$121,515 | Tax liab = $15\% \times \$1.15\text{m} \times 70\%$ = \$120,750 |

02 – Additional 15% super tax

Additional 15% super tax examples - Craig

Example – Craig

- Craig is 62 with \$4 million in superannuation at 30 June 2025. He makes no contributions or withdrawals.

Balanced asset allocation and return assumptions

Investment return assumptions

| | Asset Allocation | Capital Growth | Income | Franking Percentage | Tax free proportion | Tax deferred proportion |
|--|------------------|----------------|--------|---------------------|---------------------|-------------------------|
| Australian Equities | 19.0% | 3.9% | 4.2% | 75.0% | | |
| Prop & Alts | 19.0% | 4.3% | 3.6% | | 0.0% | 20.0% |
| Cash | 0.0% | | 2.8% | | | |
| Global Developed Fixed Interest | 24.0% | | 4.5% | | | |
| International Equities | 28.0% | 5.8% | 3.3% | | | |
| Emerging and High Yield Fixed Interest | 10.0% | | 7.0% | | | |
| | 100% | 3.18% | 4.2% | 14.3% | 0.0% | 3.8% |
| Fees - reduce income | 1.00% | | | | | |
| Earnings rate pre tax | 6.35% | 3.18% | 3.17% | | | |

Other assumptions

Holding Period in years (minimum 1)

5.00 Turnover p.a. 20%

02 – Additional 15% super tax

Additional 15% super tax examples - Craig

Example – Craig

- Craig is 62 with \$4 million in superannuation at 30 June 2025. He makes no contributions or withdrawals. By 30 June 2026 his TSB has grown to \$4.23 million.

Step 1: Earnings = $TSB_{CurrentFY} - TSB_{PreviousFY} + Withdrawals - Net\ contributions$
= \$4.23 million - \$4 million = \$230k

Step 2: Proportion of earnings = $TSB_{CurrentFY} - \$3\ million$
 $\frac{TSB_{CurrentFY}}{\$4.23\ million}$
= $\frac{\$4.23\ million - \$3\ million}{\$4.23\ million}$
= 29.1%

Step 3: Tax liability = $15\% \times Earnings \times Proportion\ of\ earnings$
= $15\% \times \$230k \times 29.1\%$
= \$10k

02 – Additional 15% super tax

Additional 15% super tax examples - Craig

Example – Craig \$4.0 million ‘balanced’ asset allocation

| All values \$'000 | Opening TSB | Divs & income rec'd (less 1% fee) | Total capital gains | Net tax on income less fees | Tax on realised gains (20% T/O) | Total tax payable (current system) | Closing Balance (\$'000) | Prov for tax on un-realised gains | Closing TSB | Extra 15% super tax |
|--|--------------|-----------------------------------|---------------------|-----------------------------|---------------------------------|------------------------------------|--------------------------|-----------------------------------|-------------|---------------------|
| Australian Equities | 760 | 24 | 30 | -5.1 | 0.6 | -4.5 | 819 | 2.4 | 816 | 2.4 |
| Property and Alternatives | 760 | 19 | 33 | 2.1 | 0.7 | 2.8 | 809 | 3.2 | 806 | 2.0 |
| International Equities | 1,120 | 25 | 65 | 3.7 | 1.3 | 5.0 | 1,205 | 5.2 | 1,200 | 3.5 |
| Global Developed Fixed Interest | 960 | 33 | - | 5.0 | - | 5.0 | 988 | - | 988 | 1.2 |
| Emerging and High Yield Fixed Interest | 400 | 24 | - | 3.5 | - | 3.5 | 421 | - | 421 | 0.9 |
| Cash | - | - | - | - | - | - | - | - | - | - |
| Total | 4,000 | 125 | 128 | 9.2 | 2.6 | 11.8 | 4,241 | 10.8 | 4,230 | 10.0 |

02 – Additional 15% super tax

Additional 15% super tax examples - Craig

Summary:

- Usual super tax liabilities: \$12k
- Cash flow after usual tax liabilities and fees: \$113k
- Extra 15% tax: \$10k

Taxation based on receipts/realisation

Taxation based on accruals

Policy proposal discussion points:

1. Indexation of \$3m threshold
2. DB interest complications
3. Carry forward losses (vs tax credit)
4. Taxation of unrealised gains

Move excess outside of super?

| Tax rate | Additional tax paid compared to 100% in super | |
|--------------------|---|--|
| | Craig example: \$1.2m outside super | \$9.0m example: \$6.2m outside super (balanced allocation returns) |
| Personal MTR 47% | \$8k | \$41k |
| Personal MTR 39% | \$3k | \$16k |
| Personal MTR 34.5% | \$1k | \$3k |
| Personal MTR 21% | -\$7k (ie tax saving) | -\$39k (ie tax saving) |

Insurance Bond option:

- Tax paid at 30% after 10 yrs
- No CGT discount
- Equivalent to MTR ~39%

Breakeven personal MTR with super +15% accruals tax:

- MTR ~33% (50% CGT discount)

Polling question 3

Do you agree with an additional tax (in any form) being applied to super balances over \$3m?

a. Yes

b. No

QAR final report and additional 15% super tax

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May 2023

