



PS LA 2021/D3 - Superannuation - Commissioner's discretion where members receive benefits in breach of legislative requirements

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 For information about the status of this draft Law Administration Practice Statement, see item 3975 on our [Advice under development program](#).



Superannuation – Commissioner's discretion where members receive benefits in breach of legislative requirements

This Law Administration Practice Statement explains when and how to exercise the discretion in subsection 304-10(4) of the *Income Tax Assessment Act 1997* where a member receives superannuation benefits in breach of legislative requirements.

This Practice Statement is a draft for consultation purposes only. When the final Practice Statement issues, it will have the following preamble:

This Practice Statement is an internal ATO document, and is an instruction to ATO staff.

1. What is this draft Practice Statement about?

This draft Practice Statement¹ sets out when and how to apply the discretion in section 304-10 of the *Income Tax Assessment Act 1997* (ITAA 1997) where a taxpayer receives a superannuation benefit from a complying superannuation fund in breach of legislative requirements.²

If the Commissioner exercises the discretion, the superannuation benefit will not form part of the person's assessable income under section 304-10, but will instead be taxed as a superannuation benefit.³

This Practice Statement outlines:

- what the discretion is for
- the legislative history and context of section 304-10, and
- principles for considering the discretion.

The Appendix to this Practice Statement includes more detail about the factors that may or may not be relevant when you are considering the exercise of the discretion.

This Practice Statement does not deal with superannuation benefits received from approved deposit funds or non-complying superannuation funds.

2. The discretion

Generally, superannuation benefits are taxed at a lower rate than income included in the person's assessable income. Divisions 301, 302 and 303 set out

the tax treatment of superannuation benefits received from complying superannuation funds.

These rules, however, do not apply where a person receives a payment from a complying superannuation fund (or the benefit was attributable to the assets from such a fund) and:

- the fund was not (when the benefit was received) maintained as required by section 62 of the *Superannuation Industry Supervision Act 1993* (SISA) (the sole purpose test), or
- the person received the benefit otherwise than in accordance with the payment standards in subsection 31(1) of the SISA.⁴

In these circumstances, the benefit is included in the person's assessable income.⁵ However, to the extent that we consider this unreasonable, we may exercise a discretion that the amount is not included in the person's assessable income under Division 304. When exercising the discretion, we consider:

- the nature of the fund, and
- any other relevant matters.⁶

This may be for the whole or part of the superannuation benefit.

The part of the benefit you exercise the discretion for remains assessable but is subject to the relevant tax treatment set out in Divisions 301, 302 or 303.⁷ That part of the benefit, therefore, may be subject to less tax than it would have been if included under section 304-10.

¹ All later references to 'this Practice Statement' refer to the Practice Statement as it will read when finalised. Note that this Practice Statement will not take effect until finalised.

² All legislative references in this Practice Statement are to the ITAA 1997, unless otherwise indicated.

³ See draft Taxation Determination TD 2021/D6 *Income tax: tax treatment of a superannuation benefit when the Commissioner exercises the discretion in subsection 304-10(4) of the Income Tax Assessment Act 1997*.

⁴ Subsection 304-10(1).

⁵ Subsection 304-10(1).

⁶ Subsection 304-10(4).

⁷ See TD 2021/D6. If a superannuation income stream that commenced on or after 20 September 2007 is payable, but any of the requirements in the *Superannuation Industry (Supervision) Regulations 1994* relating to payments from it are not met, the superannuation income stream will be taken to have ceased for income tax purposes at the start of the year. Any payments made in relation to it during the income year will be superannuation lump sums. See Taxation Ruling TR 2013/5 *Income tax: when a superannuation income stream commences and ceases*.

3. Legislative history and context of section 304-10

The superannuation system allows individuals to provide for their retirement or to provide for their dependants in the event of their death.

Division 304 is an integrity mechanism for the superannuation system. It creates a disincentive for withdrawing superannuation benefits in breach of the SISA and the *Superannuation Industry (Supervision) Regulations 1994* (SISR) payment standards by ensuring members pay a higher rate of tax on those superannuation benefits.

Subsection 304-10(4) allows the Commissioner to exercise a discretion that the amount not be included in the person's assessable income. If the discretion is exercised, the amount will be assessed under either Divisions 301, 302 or 303.

Section 304-10 is intended to ensure that the payment of excessive or unauthorised benefits is subject to tax unless the Commissioner is satisfied this would be unreasonable in the circumstances. The Commissioner's discretion in subsection 304-10(4) should generally be exercised where:

- there are no tax avoidance implications, and
- 'the excessive benefit arose fortuitously or in other circumstances beyond the effective control of the recipient or the employer'.⁸

The legislative history of section 304-10 and its predecessor, section 26AFB of the ITAA 1936, was succinctly set out in *Mason and Commissioner of Taxation* [2012] AATA 133 (*Mason*)⁹. In particular, in considering the objects of the SISA, which provides for the supervision of superannuation funds by the relevant regulators, the Administrative Appeals Tribunal (AAT) noted that an important element of the scheme of regulation is the deterrent effect of legislative provisions, including section 304-10.

The AAT also noted¹⁰ three consequences that can flow from a breach of the SISA, being:

- the superannuation fund can be made non-complying
- the trustees of the fund can be disqualified, and/or
- the benefit can be treated as assessable income in the hands of the taxpayer.

The AAT concluded that these consequences are an integral part of the regulator regime which has the

purpose of encouraging prudent investment to meet the policy objectives.¹¹

4. Principles for considering the discretion

You must consider all the relevant facts and circumstances surrounding the receipt of the superannuation benefit. Consider the circumstances as a whole, rather than each factor in isolation. To exercise the discretion, you need to be satisfied that it would, on balance, be unreasonable for the superannuation benefit to be included in the person's assessable income under Division 304.

When exercising the discretion, subsection 304-10(4) requires you to consider:

- the **nature of the fund** the superannuation benefit is paid from – different weighting may need to be given to particular factors depending on whether the fund from which the benefit was received is a self-managed superannuation fund (SMSF) or an Australian Prudential Regulation Authority (APRA)-regulated fund, and
- any other matters the Commissioner considers relevant.

The following factors will help you to determine how to exercise the discretion. They are discussed in more detail (including case law) in the Appendix to this Practice Statement.

Factors that may support exercising the discretion favourably

The nature of the fund is a factor, as it affects how much effective control the recipient of a benefit has. If a benefit arises in circumstances that are genuinely out of the effective control of the person, this may support you exercising the discretion in their favour.

SMSFs – All members of an SMSF are required to be trustees of the fund or directors of the fund's corporate trustee. We expect them to have effective control over the SMSF's management, and the amount and timing of all benefit payments paid from the SMSF.

APRA-regulated funds – By contrast, these funds have trustees or administrators who are generally expected to be acting at arm's length from the members. This means the members are less likely to have effective control over the superannuation fund's management and payment of benefits.

⁸ See the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 4) 1987, which provides context for the operation of former section 26AFB of the *Income Tax Assessment Act 1936* (ITAA 1936), which was replaced by section 304-10.

⁹ *Mason* at [24–26].

¹⁰ *Mason* at [30].

¹¹ *Mason* at [30].

There may be some limited situations where an SMSF member does not have effective control over the amount paid from the SMSF. This would include, for example, where a bank made an error and paid more from a transition to retirement pension than was requested by the member.

Factors that may not provide support for exercising the discretion favourably

Factors that will have little or no weight when deciding whether to exercise the discretion include:

- the person was suffering **financial hardship or distress** when accessing the benefit (for example, where the person borrows money from the superannuation fund to maintain their business or family home)
- **attempted rectification** of the transaction by paying an amount equivalent to the superannuation benefit to the superannuation fund immediately or shortly after receiving the benefit¹²
- **disqualification** of the person from being a **superannuation fund trustee** – this is a regulatory consequence resulting from the person not complying with the provisions of the SISA and/or being found to not be a fit and proper person to be a trustee¹³; it should not be

taken to be a penalty for the purposes of exercising the discretion

- the **tax consequences under Division 304 are undesirable or difficult for the person** to meet – these are an important deterrent to ensure the integrity of the superannuation system.

If a superannuation benefit has been accessed under an illegal early release scheme, we generally would not exercise the discretion. This is the case even where the person loses the benefit of the funds due to fraudulent activity committed by another person (for example, the promoter of the scheme) after it has been released.

In addition to these factors, you may consider any other **factors present when the amount was paid**, but give little weight to anything that occurs after that time. This includes factors that are unforeseen, or that are outside the person's control, such as a significant global financial downturn.

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| Date issued | 15 December 2021 |
| Date of effect | When finalised, this Practice Statement will apply from the date of publication. |
| Contact officer | Sharon Russell |

¹² If the amount is paid back into the fund, it will be a contribution (see *Taxation Ruling TR 2010/1 Income tax: Superannuation contributions*). The ordinary rules will

apply to determine if the contribution counts towards the concessional or non-concessional contribution caps.

¹³ See section 126A of the SISA.

APPENDIX 1

This Appendix provides further background around factors that may provide, or may not provide, support for exercising the discretion in favour of a person.

5. Factors that may provide support for exercising the discretion in favour of a person

Effective control and the nature of the fund

A factor that may support exercising the discretion in favour of a person is where the benefit received arose in circumstances that were genuinely out of their effective control.¹⁴

The nature of the fund will be relevant when considering the effective control of the recipient of the superannuation benefit.

Section 17A of the SISA sets out the basic conditions that a fund must meet for it to be an SMSF. A key requirement of section 17A is that each member must be a trustee or a director of the corporate trustee of the fund. Accordingly, '... all SMSF members/trustees have 'effective control' over prudential management of their funds' assets and the amount and timing of all benefit payments emanating from their fund' (*Mason* at [34]). This may be contrasted with a member of a large APRA fund.

This is consistent with the comments of Logan J in *Raelene Vivian, suing in her capacity as the Deputy Commissioner of Taxation (Superannuation) v Fitzgeralds* [2007] FCA 1602:

25. Our Parliament has deliberately constructed a scheme whereby, in return for submission to a regulatory regime found in the SISA, particular taxation benefits are given to the trustee of a superannuation fund and its members. The public policy that seems to underlie that particular concession is to encourage prudent provision by Australians for their retirement. In so doing, the burden on other Australian taxpayers in the provision of social security benefits for the aged is thereby lessened. I can, I believe, responsibly take judicial notice that a contemporary phenomenon is a recognition that Australia has, in terms of its demographics, a need for such provision to be encouraged.

26. Part of the scheme found in the legislation is to enable what one might term small funds or, at least, funds which have fewer than five members to be self-managed. That is a particular benefit conferred by the Parliament on those who would wish to make provision for their retirement. It enables self-management as opposed to becoming a member of a fund the management of which may be remote from membership. It is a privilege. It is a privilege that that [sic] should not be abused. It's quite plain to me that in this case that that privilege has been abused. I am in no doubt whatsoever that, in terms of the legislation, this particular case is one in respect of which I can be satisfied that there have been contraventions which are, in terms of section 196 subsection (4) of the SISA, serious.

It is expected that all trustees of an SMSF will be aware of all the relevant requirements of the SISA and the SISR pertaining to the payment of benefits, including:

- whether a member has met a condition of release
- any cashing conditions attached to a particular condition of release
- annual amounts required to be paid from a superannuation income stream, including any limits on the annual amount that may be paid
- restrictions as to the commutation of various pension types, and
- obligations with respect to release authorities.

It is in this context that you must consider whether circumstances are genuinely beyond the 'effective control' of the recipient of the benefit where the benefit is paid from an SMSF.

An example of a benefit received genuinely beyond the recipient's effective control would be where the member is in receipt of a transition to retirement income stream and a transposition error by the SMSF's bank in responding to a request for payment leads to an amount in excess of the 10% annual limit being inadvertently paid.

A member of a small APRA fund or a large APRA fund is less likely to have effective control where they have no involvement in the operation of the fund, such as where there is an arm's length relationship between the member and the trustee or administrator of the fund.¹⁵

¹⁴ *Mason* at [31].

¹⁵ *Mason* at [34].

6. Factors that may not provide support for exercising the discretion in favour of a person

Factors that will have little or no weight when deciding whether to exercise the discretion are discussed in further detail below.

Suffering financial hardship

The fact the person may have been suffering from financial distress or hardship at the time they received the benefit is generally a factor that would be given little or no weight when deciding to exercise the discretion.

This includes where a person borrows money from the fund to maintain their business or family home. The assets of a superannuation fund are not to be used as 'a lender of last resort'.¹⁶

This is consistent with the view expressed by the AAT in *Sinclair and Commissioner of Taxation* [2012] AATA 634 at [73]:

While the circumstances of the Applicant are clearly difficult, they are not sufficient to call into play the exercise of the discretion conferred on the Respondent by s 304-10(4). Preserving funds within the superannuation system and not having them accessed by members before retirement is the key driver behind the superannuation system, and the reason why early access possibilities are so carefully prescribed in Regulation 6.17(2) of the SISR and Schedule 1 of those Regulations. Mere financial difficulties experienced by members cannot be enough to bring the discretion into play.

Other provisions in the law provide an avenue for those in financial hardship to access superannuation benefits, such as the 'severe financial hardship' or 'compassionate ground' conditions of release.¹⁷

Individuals considering accessing their superannuation entitlements in these circumstances should consider whether they qualify under these grounds, and apply to access benefits under them if appropriate. However, if they have accessed superannuation benefits without meeting the requirements of those conditions of release, the fact they are suffering financial hardship is generally not a factor that would support exercising the discretion.

Attempted rectification of the transaction

A member's attempt to rectify a transaction by paying an amount equal to the superannuation benefit to the superannuation fund, immediately or shortly after receiving the benefit, is generally a factor that would be given little or no weight when considering whether to exercise the discretion. This includes where the payment is properly recorded as a concessional or non-concessional contribution.

The payment of monies to a fund after an amount has been paid from the fund can have no effect on whether or not that amount was paid in breach of the SISA/SISR requirements. In particular, the payment to the fund does not unwind the original payment from the fund. Whether the discretion should be exercised should be based on considerations directly related to the payment itself.

Disqualification of the person from being a trustee

Disqualification¹⁸ of the person should not be taken to be a penalty for the purpose of exercising the discretion. This is because disqualification is not a taxation consequence flowing from the person accessing superannuation benefits in breach of legislative requirements. It is a regulatory action resulting from the person not complying with the provisions in the SISA and/or otherwise not being a fit and proper person.¹⁹ It is therefore not a factor that would generally give weight to exercising the discretion.

¹⁶ See *Smith and the Commissioner of Taxation* [2011] AATA 563 at [21]; *Raelene Vivian, suing in her capacity as the Deputy Commissioner of Taxation (Superannuation) v Fitzgeralds* [2007] FCA 1602; *ZDDD and Commissioner of Taxation* [2011] AATA 3.

¹⁷ Superannuation benefits may be paid due to severe financial hardship under table item 105 to Schedule 1 of the SISR or due to compassionate grounds under table item 107 to Schedule 1 of the SISR.

¹⁸ Section 126A of the SISA.

¹⁹ Law Administration Practice Statement PS LA 2006/17 *Self-managed superannuation funds – disqualification of individuals to prohibit them from acting as a trustee of a self-managed superannuation fund* provides guidance on deciding whether to disqualify individuals.

The taxation consequences are difficult for the person to meet, or undesirable

The fact that the taxation consequences of not exercising the discretion may be difficult for a person to meet or undesirable for that person is not a factor that should give weight to exercising the discretion. This is consistent with the view expressed by the AAT in *Mason* at [32]:

However, it will *not* be “unreasonable” to include a superannuation benefit in a person’s assessable income (to be taxed at marginal tax rates) merely because the taxation consequence prescribed by Parliament is difficult for the taxpayer to meet, or is regarded by the taxpayer as undesirable. If this were so, the important deterrent effect of section 304-10 of the ITAA 1997 would be undermined and an unintended taxation benefit would thereby be conferred on the recipient of the payment.

Illegal early access schemes

The involvement of a person in an illegal early access scheme will be a factor against exercising the discretion in subsection 304-10(4).

This is the case even where the person loses the benefit of the funds due to fraudulent activity committed by another person (for example, the promoter of the scheme) after it has been released. Where the scheme involved the rollover of a benefit to another superannuation fund a person is required to make reasonable enquiries to ensure the receiving fund is a bona fide fund.

This is consistent with the view expressed by the AAT in *Brazil and Commissioner of Taxation* [2012] AATA 192 at [34]:

I do not accept that such an argument could apply in the applicant’s case. Mr Brazil suspected (or should have suspected) that the Fund was not a *bona fide* superannuation fund. He made no effort to find out information about the Fund and why he could receive his superannuation benefit from the Fund, when he could not receive it from the AON Master Trust. He did not worry or care about this. As he said in his evidence, he needed the money and he was prepared to do anything to get it. Others had done it that way and received the early release of their superannuation benefits and he was content to proceed in the same way. He believed that tax had been deducted from the payment and remitted to the respondent. However, he had no evidence of this and did not seek to obtain any documentation to show what had been withheld and remitted. As Mr Cole submitted further, the exercise of the discretion in the applicant’s favour would mean that the tax-paying community would be footing the tax bill in circumstances where there was no documentation to show that any tax had been paid.

It is also consistent with the view expressed by the AAT in *Vuong and Commissioner of Taxation* [2014] AATA 402 (*Vuong*):

33. In this regard, the applicant contended that he intended to roll over his superannuation benefit to a complying superannuation fund. The respondent countered this by pointing to previous statements made by the applicant indicating that he intended to access his superannuation early. In the Tribunal’s opinion, neither of these submissions is ultimately to the point. The Tribunal accepts that it was always the applicant’s intention to access his superannuation early, but the Tribunal does not accept that he intended to do so unlawfully.

34. The applicant was ignorant as to the law and was led to believe that if he rolled over his superannuation from one fund to another, a consequence would be that he would have a lawful entitlement to access it. His ultimate, albeit naïve, objective is not relevant in this context – the fact is that he received the payment when the Equisuper cheque was deposited in the fraudulent bank account and, being a benefit received otherwise than in accordance with the SIS Regulations, the full amount of that deposit should have been included in his assessable income.

Events that occur after the superannuation benefit has been received

Generally, matters that occur after the superannuation benefit was accessed should be given little or no weight in determining whether to exercise the discretion. This includes where the event was unable to be foreseen, or was out of the control of the person; for example, a significant global financial downturn.²⁰

In *Vuong*, the applicant was unwittingly enticed into an arrangement to gain early release of his superannuation benefits from an APRA-regulated fund. Evidence was given of medical expenses incurred by the applicant in respect of his wife and parents. In considering whether this evidence supported a conclusion that the applicant actually

²⁰ Decision Impact Statement on *Wainwright and Commissioner of Taxation* [2019] AATA 333.

qualified for the early release of his benefits under the compassionate grounds condition of release (table item 107 to Schedule 1 of the SISR), the AAT (in concluding that the evidence did not) observed at [40]:

These circumstances are not relevant in the present context because it was acknowledged by the applicant under cross-examination that the events all occurred subsequent to his receipt of the benefit.

The Commissioner considers that this view, as a matter of general principle, can apply equally in the context of a consideration whether to exercise the discretion in section 304-10(4).

APPENDIX 2 – YOUR COMMENTS

You are invited to comment on this draft Practice Statement, including the proposed date of effect. Please forward your comments to the contact officer by the due date.

A compendium of comments is prepared when finalising this Practice Statement, and an edited version (with names and identifying information removed) may be published to the Legal database on ato.gov.au. Please advise if you do not want your comments included in the edited version of the compendium.

Due date: 4 February 2022

Contact officer details have been removed.

References

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| Legislative references | ITAA 1997 Div 301 ITAA 1997 Div 302 ITAA 1997 Div 303 ITAA 1997 Div 304 ITAA 1997 304-10 ITAA 1997 304-10(1) ITAA 1997 304-10(4) ITAA 1936 former 26AFB SISA 1993 17A SISA 1993 31(1) SISA 1993 62 SISA 1993 126A SISR 1994 6.17(2) SISR 1994 Schedule 1 SISR 1994 item 105 of Schedule 1 SISR 1994 item 107 of Schedule 1 |
| Case references | Brazil and Commissioner of Taxation [2012] AATA 192; 2012 ATC 10-244; (2012) 88 ATR 277 Mason and Commissioner of Taxation [2012] AATA 133; 2012 ATC 10-237; (2012) 87 ATR 326 Raelene Vivian, suing in her capacity as the Deputy Commissioner of Taxation (Superannuation) v Fitzgeralds [2007] FCA 1602; 2007 ATC 5105; (2007) 69 ATR 834 Sinclair and Commissioner of Taxation [2012] AATA 634; 2012 ATC 10-275; (2012) 90 ATR 719 Smith and the Commissioner of Taxation [2011] AATA 563; 2011 ATC 10-197; (2011) 84 ATR 667 Vuong and Commissioner of Taxation [2014] AATA 402; 2014 ATC 10-367; (2014) 98 ATR 910 ZDDD and Commissioner of Taxation [{2011] AATA 3; (2011) 81 ATR 872; (2011) 122 ALD 164 |
| Other references | DIS on Wainwright and Commissioner of Taxation [2019] AATA 333 Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 4) 1987 |
| File references | 1-I3B46VY |
| Related public rulings | TR 2010/1 TR 2013/5 TD 2021/D6 |
| Related practice statements | PS LA 2006/17 |

ATO references

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