EXPLANATORY STATEMENT

Social Security (Guidelines for Determining whether Income Stream is Asset-test Exempt) (DEWR) Determination 2007 (No 1)

Summary

The Social Security (Guidelines for Determining whether Income Stream is Asset-test Exempt) (DEWR) Determination 2007 (No 1) (the Determination) are made under subsections 9A(6) and 9B(5) of the *Social Security Act 1991* (the Act).

The purpose of the Determination is to specify circumstances in which certain income streams retain their 100% exemption from the assets test under the Act.

Background

Subsections 9A(6) and 9B(5) allows the Secretary to determine guidelines for the purpose of making a determination under subsections 9A(5) and 9B(4) respectively that an income stream is an asset-test exempt income stream.

The Determination covers certain income streams (the 'new income stream') that are purchased or acquired as the result of the commutation or rollover of a 100% assets-test exempt income stream covered by subsections 9A(1), 9A(1A) and 9B(1) that were purchased or acquired before 20 September 2004 (the 'original income stream').

If the new income stream is purchased or acquired on or after 20 September 2007, and the income stream is covered by the Determination, the new income stream will retain the 100% exemption that applied to the original income stream (whether the original income stream was purchased before 20 September 2004 or was commuted and rolled over to another income stream between 20 September 2004 and 19 September 2007), provided it was commuted or rolled over from, and retains the features of the original income stream. The effect of not being covered by the Determination is that these income streams will lose the 100% exemption altogether, even if they retain the features of the original income stream.

Explanation of the Provisions

Section 1 states the name of the Determination is the *Social Security (Guidelines for Determining whether Income Stream is Asset-test Exempt) (DEWR) Determination 2007 (No 1).*

Section 2 sets out that the Determination commences on 20 September 2007.

Section 3 provides definitions of terms used in the Determination.

Section 4 sets out the purpose of the Determination, namely to set out guidelines with which the Secretary must comply when making a determination under subsection 9A(5) or 9B(4) of the Act regarding certain income streams commencing on or after 20 September 2007.

The section includes a note to the effect that, under subsection 9A(5) or 9B(4) of the Act, the Secretary may determine that an income stream is an asset-test exempt income stream.

Section 5 sets out various income streams that are covered by the Determination and were purchased on or after 20 September 2007 which may be determined to be an asset-test exempt income stream for the purposes of the Act.

Any income stream covered by section 5 must meet the requirements of **subsection 5(1)** of the Determination: that is, it (referred to as the ‘present income stream’) must be covered by section 9A or 9B of the Act (or would have been covered by those provisions if paragraph 9A)(1)(aa) and subparagraph 9B(1)(a)(i) of the Act did not apply) and must be purchased by the primary beneficiary on or after 20 September 2007 from the commutation of an asset-test exempt income stream originally purchased before 20 September 2004 (referred to in the section as the ‘original income stream’). A commutation is lump sum withdrawal of capital from the assets backing the income stream. Commutations are separate from any regular income payments that are paid from the income stream.

In addition, the original income stream must meet the more specific requirements of one of the following subsections 5(2) to (5).

Subsection 5(2) sets out that the subsection applies to an original income stream if it is covered by either subsection 9A(1) or (1A) or section 9B of the Act and, if:

- the income stream was purchased for the benefit of the primary beneficiary and a reversionary beneficiary; and
- payments under the original income stream were based on the reversionary beneficiary’s life expectancy; and
- that reversionary beneficiary has died before the primary beneficiary (that is, the primary beneficiary purchases a lifetime income stream and specifies that it must revert to the reversionary beneficiary who has a longer life expectancy at the time of purchase but predeceases the person who purchase the income stream).

Subsection 5(3) sets out that the subsection applies to an original income stream if it is covered by either subsection 9A(1) or (1A) or section 9B of the Act and is not covered by section 8 or 9 of the Determination (payment splits and Family Court Orders). The original income stream must also have been purchased by the primary beneficiary for the benefit of both him or herself and a reversionary beneficiary who are members of a couple at the time of the purchase, but who subsequently part.

Subsection 5(4) sets out that the subsection applies to an original income stream which is a defined benefit pension covered by section 9A or 9B provided by a regulated superannuation fund and in relation to which the Secretary is not satisfied as required by paragraph 9A(1)(b) or 9B(1A)(b) (that is, the Secretary is not satisfied that there is in place a current actuarial certificate setting out that in the actuary’s opinion there is high probability that the income stream’s provider will be able to pay the income stream as required under the income stream’s contract or governing rules).

Subsection 5(5) sets out that the subsection applies to an original income stream which is an immediate annuity under a statutory fund established by a life company, or under a benefit fund, and the original income stream is **either**:

- an income stream to which the Secretary is not satisfied as required by paragraph 9A(1)(b) or 9B(1A)(b) of the Act (that is, the Secretary is not satisfied that there is in place a current actuarial certificate setting out that in the actuary's opinion there is high probability that the income stream's provider will be able to pay the income stream as required under the income stream's contract or governing rules); **or**
- the income stream fails to satisfy the relevant standards published by the Australian Prudential Regulation Authority about minimum surrender values and paid up values.

Section 6 is similar to section 5, with one additional provision, and sets out various income streams that are covered by the Determination and were purchased on or after 20 September 2007 which may be determined to be an asset-test exempt income stream for the purposes of the Act.

Any income stream covered by section 6 must meet the requirements of **subsection 6(1)** of the Determination: that is, the new asset-test exempt income stream (referred to in the section as the 'present income stream')must be covered by section 9A or 9B (or would have been covered by those provisions if paragraph 9A)(1)(aa) and subparagraph 9B(1)(a)(i) of the Act did not apply) and must have been sourced from an intermediate asset-test exempt income stream created on or after 20 September 2004 and before 20 September 2007 that itself had been created from an earlier asset-test exempt income stream created before 20 September 2004 (referred to in the section as the 'original income stream'). All three income streams must be covered by section 9A or 9B of the Act.

A commutation is a lump sum withdrawal of capital from the assets backing the income stream. Commutations are separate from any regular income payments that are paid from the income stream.

In addition, the original income stream must meet the more specific requirements of one of the following subsections 6(2) to (5).

Subsection 6(2) sets out that the subsection applies to an original income stream if it is covered by either subsection 9A(1) or (1A) or section 9B of the Act and, if:

- the income stream was purchased for the benefit of the primary beneficiary and a reversionary beneficiary; and
- payments under the original income stream were based on the reversionary beneficiary's life expectancy; and
- that reversionary beneficiary has died (that is, a person purchases a lifetime income stream and specifies that it must revert to his or her partner (who has a longer life expectancy at the time of purchase), however the partner predeceases the person who purchase the income stream).

Subsection 6(3) sets out that the subsection applies to an original income stream is if it is covered by either subsection 9A(1) or (1A) or section 9B of the Act and is not covered by section 8 or 9 of the Determination (payment splits and Family Court Orders). The original income stream must also have been purchased by the primary beneficiary for the benefit of both him or herself and a reversionary beneficiary who are members of a couple at the time of the purchase, but who subsequently part.

Subsection 6(4) sets out that the subsection applies to an original income stream which is a defined benefit pension covered by section 9A or 9B that is provided by a regulated superannuation and in relation to which the Secretary is not satisfied as required by paragraph 9A(1)(b) or 9B(1A)(b) (that is, the Secretary is not satisfied that there is in place a current actuarial certificate setting out that in the actuary's opinion there is high probability that the income stream's provider will be able to pay the income stream as required under the income stream's contract or governing rules).

Subsection 6(5) sets out that the subsection applies to an original income stream whcih is an immediate annuity under a statutory fund established by a life company, or under a benefit fund, and the original income stream is **either**:

- an income stream to which the Secretary is not satisfied as required by paragraph 9A(1)(b) or 9B(1A)(b) of the Act (that is, the Secretary is not satisfied that there is in place a current actuarial certificate setting out that in the actuary's opinion there is high probability that the income stream's provider will be able to pay the income stream as required under the income stream's contract or governing rules); **or**
- the income stream fails to satisfy the relevant standards published by the Australian Prudential Regulation Authority about minimum surrender values and paid up values.

Sections 7 to 13 of the Determination set out additional conditions for retaining the 100% asset-test exemption for various income streams that were covered by the Determination and were purchased on or after 20 September 2007.

Income streams covered by **sections 7 to 13** must be covered by section 9A or 9B of the Act, have been purchased on or after 20 September 2007 and must be purchased from the proceeds of the commutation of an asset-test exempt income stream (the 'original income stream'). The original income stream must have been:

- purchased before 20 September 2004; or
- resulted from the proceeds of the commutation of an asset-test exempt income stream, or a succession of asset-test exempt income streams where the first income stream in the succession of income streams was purchased before 20 September 2004.

A commutation of a lump sum withdrawal of capital from the assets backing the income stream. Commutations are separate from any regular income payments that are paid from the income stream.

The fundamental difference between sections 5 and 6 of the Determination and sections 7 to 11, is that the 'original income stream' can be commuted and rolled over only once under the Determination specified in sections 5 and 6, that is, the ‘original income stream’ will not have been sourced from a previous income stream. By contrast, under sections 7 to 11, the ‘original income stream’ may be one of a succession of intermediate income streams that itself has been sourced from the commutation and rollover of a previous ‘original income stream’ under the 2005 Principles or this Determination, as specified in those sections.

In these circumstances, the full (100%) exemption from the assets test would carry through to the new income stream. A further requirement of these sections is that the capital used to source the intermediate income stream and the new income stream must have originated only from the previous commuted income stream that is, it would not be permissible to increase this capital with assets from elsewhere, thus increasing the purchase price of the new income stream.

Section 7 of the Determination covers an income stream where it results from the transfer of the original income stream to a successor fund on or after 20 September 2007 (“successor fund” is defined in subregulation 1.03(1) of the *Superannuation Industry (Supervision) Regulations 1994*). The original income stream must have been provided by a regulated superannuation fund (“regulated superannuation fund” is defined in section 19 of the *Superannuation Industry (Supervision) Act 1993).*

Sections 8 and 9 of the Determination cover various income streams that are commuted because of the operation of the *Family Law Act 1975* (the Family Law Act). The purpose of these sections is to ensure that the full exemption from the assets test is carried through to any new income streams sourced from the commutation of an original income stream, because of the operation of the Family Law Act.

Section 8 covers an income stream that has been purchased or acquired by the primary beneficiary or his or her spouse on or after 20 September 2007, and the income stream results from the original income stream being commuted as a result of a payment split under Part VIIIB of the Family Law Act.

Section 9 covers an income stream that has been purchased or acquired by the primary beneficiary or his or her spouse on or after 20 September 2007, and the income stream results from the original income stream being commuted as a result of:

- an order made under either section 79 or 114 of the Family Law Act; or
- an injunction that has been granted under section 114 of that Act that is binding on a third party (such as the income stream provider) under Part VIIIAA of that Act; or
- any other order or injunction under the Family Law Act that relates specifically to the original income stream.

Section 10 of the Determination covers an income stream that has been purchased by the primary beneficiary on or after 20 September 2004, and which results from the commutation of the original income stream to pay a superannuation contributions surcharge debt.

Section 11 of the Determination covers an income stream that has been purchased by the primary beneficiary and results from the commutation of the original income stream to pay a hardship amount, which is defined in subsection 9A(7) of the Act.

Section 12 of the Determination covers an income stream which was not sourced from a self managed superannuation fund, has been purchased by the primary beneficiary and results from the original income stream (sourced from a self managed superannuation fund) being commuted due to the closure of a self managed superannuation fund because:

- a member of the fund supporting the original income stream has died; or
- the administrative responsibilities of the fund supporting the original income stream have become too onerous due to the age or incapacity of a trustee.

Section 13 of the Determination covers an income stream which has been purchased by the primary beneficiary on or after 1 July 2007 and results from the original income stream being commuted and rolled over to a new income stream that is compliant with subregulation 6.21(2A) of the SIS Regulations.

This will apply in certain circumstances, such as where the contract or governing rules of the original income stream are altered to make the income stream compliant with subregulation 6.21(2A) of the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations).

Consultation

The Department of Education, Science and Training and the Department of Families, Community Services and Indigenous Affairs were consulted in relation to this instrument to ensure a co-ordinated approach in respect of payments under the Act for which they have responsibility.

Consultation regarding this instrument was undertaken with the Department of Veterans' Affairs as that Department administers legislation which incorporates similar rules relating to the treatment of income streams as that provided by the Act.

Consultation was also undertaken with the Department of the Treasury, the Australian Prudential Regulatory Authority, the Attorney-General's Department and the Investment and Financial Services Association.

Regulatory Impact Analysis

This instrument does not require a Regulatory Impact Statement (RIS) and/or a Business Cost Calculator Figure. This instrument is not regulatory in nature, will not impact on business activity and will have no, or minimal, compliance costs or competition impact. It is not expected that any compliance costs will be incurred by business against the nine categories listed as a result of this instrument.