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POLICY POINT

U.S. Taxation of Australian Retirement Accounts—A Policy Perspective

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Australian law mandates that employees in Australia participate in a retirement savings plan (the superannuation system) that is managed by Australian governmental organizations. Individual employee superannuation accounts are taxed by the Australian government at low rates. Conversely, the United States has a voluntary retirement savings system, wherein (with the exception of the Social Security benefit program and defined benefit pension systems offered to an increasingly small portion of the workforce) U.S. citizens are expected to save for their retirement. The Australian and U.S. retirement systems are structured and taxed differently. Noteworthy issues include the timing of the imposition of tax and the taxpayer on whom tax is imposed; taxation based on residency, citizenship and source of income; and the fact that there is limited guidance to assist in planning. From a tax policy perspective, the three kinds of tax complexities described by David Bradford[1] are visible in the superannuation context: there is "rule complexity" in the complexity of the relevant laws themselves; there is "compliance complexity" due to the lack of guidance as to the application of those laws, making it difficult for affected individuals to understand and comply with those laws; and there is "transactional complexity" with the choice of the Superannuation Fund (SF) structure potentially allowing for a minimization of U.S. tax exposure.

I. The Two Systems

A. The Australian Retirement System

Australian superannuation accounts are held within trusts established under Australian law to provide retirement and death benefits for members. As of December 2023, the collective value of superannuation assets was approximately AUD $3.7 trillion[2] (US $2.5 trillion).[3] These trusts are commonly structured as large industry or retail investment funds with thousands of members and professional trustees (Large Funds), or private self-managed superannuation funds (SMSFs), with up to six individual members who are also co-trustees (or co-directors of a private trustee corporation).[4]

[1] David F. Bradford, Untangling The Income Tax (1999), at 266-67.

[2] The Association of Superannuation Funds of Australia, *Super Statistics*.

[3] This uses the average exchange rate for December 2023 of 0.6645.

[4] Ato.gov.au, *Thinking about Self-managed Super*.

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The trusts are regulated by Australian government authorities[5] and are governed by statute.[6] Australian employers must contribute a percentage share of an employee's gross wages (the Superannuation Guarantee)[7] to each employee's superannuation account each quarter throughout the tenure of employment or are subjected to penalties.[8] Employees may make limited additional pre-tax (concessional) or post-tax (non-concessional) contributions.[9] Absent severe financial hardship, incapacity, or a terminal illness, account holders may only access funds upon reaching the age of 65.[10]

The superannuation system is highly tax-favored, when considering that Australia's highest marginal tax rate for residents is 47% for taxable incomes over AUD $180,000.[11] Concessional contributions are taxed (within the fund) at 15% or 30%.[12] Income and gains are taxed (within the fund) at a maximum rate of 15% during the accumulation phase while the individual is still working,[13] but distributions or withdrawals are generally tax-free.[14] Death benefits are distributed tax-free to dependents.[15] This reflects the Australian government's objective of creating a "sustainable retirement income policy which delivers fair and adequate incomes."[16]

Australian employers must contribute a percentage share of an employee's gross wages (the Superannuation Guarantee) to each employee's superannuation account each quarter.

B. The U.S. System

The U.S. has a broader range of retirement savings plans available. These include tax-favored ERISA qualified retirement plans such as defined benefit (pension) plans funded from employer contributions, which provide fixed, pre-established benefits for employees at retirement,[17] and defined contribution plans such as traditional (pre-tax) and Roth (post-tax) section 401(k) plans and individual retirement accounts (IRAs),[18] funded by contributions from employers and employees up to specified annual limits. Non-qualified plans such as Section 402(b)(1) employee benefits trusts include contributions in an employee's gross income in the year of contribution if the employee's interest was "substantially vested" at that time.[19] Vested accrued benefits of highly compensated employees are also taxable where the trust is discriminatory because it does not satisfy minimum participation

5 Australian Prudential Regulation Authority under section 4 of the *Superannuation Industry (Supervision) Act (Cth) 1993*, and the Australian Taxation Office.

6 *Superannuation Industry (Supervision) Act (Cth) 1993* and the *Superannuation Guarantee (Administration) Act (Cth) 1992*.

7 11% as of 1 July 2023, up to AUD $27,500. See ato.gov.au, *How much Super to pay*.

8 Part 3 of the *Superannuation Guarantee (Administration)Act 1992*.

9 Ato.gov.au, Growing and keeping track of your super.

10 Ato.gov.au, *Preservation Age*.

11 Ato.gov.au, *Tax rates - Australian residents*.

12 15% applies where combined income and superannuation contributions are AUD $250,000 or less; or if more, at 30%. Ato.gov.au, *Personal Super Contributions*.

13 Parliamentary Budget Office, *How is Super Taxed?* PBO Budget Explainer (Apr. 27 2023), at 10.

14 *Id.* at 7.

15 Defined to include spouses, minor children, disabled or financial dependent adult children, and persons in an interdependency relationship with the deceased). Ato.gov.au, *Superannuation Death Benefits*.

16 Treasury.gov.au: Retirement Income Modelling Task Force, *Saving For Retirement: The Benefits Of Superannuation For Individuals And The Nation*, at 2.

17 IRS.gov, *Defined Benefit Plan*.

18 K. Ashford, *What is a defined contribution plan?* Forbes Advisor (June 13, 2023).

19 Reg. § 1.402(b)-1.

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or coverage requirements. The Social Security system (a direct government benefit) is financed through a payroll tax on the earnings of the employed and self-employed: it provides retirement payments to retirees who have reached the applicable Social Security retirement age and have paid employment taxes for at least 10 years, earning work credits.[20]

The superannuation system is highly tax-favored.

C. Comparison of the Two Systems

There is no U.S. retirement plan that is equivalent to superannuation. A Roth IRA is perhaps the closest U.S. structure to a SF account, given the similarities in the taxation of contributions, distributions, and death benefits. There are differences, however, in the taxation of earnings and restrictions on the withdrawal of benefits.

SFs also have similarities to non-exempt trusts as a SF account holder's interest is arguably "substantially vested" – i.e. transferable or not subject to a substantial risk of forfeiture.[21] A SF account holder has a defined interest in their account each day, may transfer the account balance to another fund, and has no risk of forfeiture, as the account is held solely for their benefit even if funds may only be accessed in the future.[22] The IRS applied Section 402(b) to Singaporean Central Provident Funds which have similar features to SFs, such as compulsory contributions and withdrawal limitations.[23] While extending similar tax treatment to SFs may seem reasonable, the IRS has not discussed how the rules apply to foreign trusts generally.[24] Because the rules were enacted to deter employers from establishing plans that discriminated against non–highly compensated employees,[25] their application is unclear to trusts with mandatory contribution requirements for *all* employees that negate any grounds for discrimination.[26]

Some commentators consider the Australian Superannuation Guarantee to be comparable to the U.S. Social Security taxes payable by employers under the Federal Insurance Contributions Act (FICA) and the Self-Employment Contributions Act (SECA). Like the Superannuation Guarantee, those do not apply when employee wages are subject to the social security system of a foreign country under a totalization agreement with the U.S.[27]

Some commentators consider the Australian Superannuation Guarantee to be comparable to the U.S. Social Security taxes.

[20] SSA.gov, *How is Social Security Financed?* and *Social Security Credits*.
[21] Reg. § 1.83-3.
[22] Reg. § 1.83-3(b).
[23] IRS.gov, IRS Internal Memorandum *Singapore Central Provident Fund*, October 10, 1997, and Ato.gov.au, *Withdrawing and Using Your Super*.
[24] Rev. Rul. 2007-48 *Section 402. Taxability of Beneficiary of Employees' Trust*.
[25] Mary R. Jones, *Sec.402(b) and Foreign Pension Plans*, The Tax Adviser (Mar 1, 2012).
[26] § 401(a)(26).
[27] *See* IRS, *Totalization Agreements* (describing bilateral agreements to eliminate dual coverage); Marsha Laine Dungog and Tamara Cardan, *Dixon: A Cautionary Case of U.S.-Australian Tax Issues* (Feb 22, 2021).

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Table 1. Comparison of Taxation of Retirement Accounts

Taxing Point	Australia[28]		U.S. Qualified Plans[29]		U.S. Other	
	Concessional (pre-tax)	Nonconcessional (post-tax)	Traditional IRA/401(k)	Roth IRA/401(k)	402(b) Non-exempt Trusts	Social Security[30]
Contributions	15% or 30%[31]	Marginal tax rate (pre-contribution)	0%	Marginal tax rates (pre-contribution)	Marginal tax rates if substantially vested[32]	6.2% - 12.4%
Earnings	15% (in fund) during accumulation	15% (in fund) during accumulation	0%[33]	Tax free[34]	Vested accrued benefits may be taxable[35]	N/a
Distributions/ withdrawals	Generally, 0% if over age 60	Generally, 0% if over age 60	Marginal tax rate[36]	Tax-free qualified withdrawals[37] (or tax + 10% penalty).	Generally tax-free[38]	Up to 85% at marginal tax rate. Remainder taxfree[39]
Death benefits	0% if paid to a super-annuation dependent	0% if paid to a superannuation dependent	Beneficiary's marginal tax rate[40]	May be inherited income-tax-free[41]		Taxable if survivor's income > USD $25,000[42]

II. The Cross-National Issues

Two categories of individuals are affected by the currently unsettled state of the law: (1) Australian nationals living in the U.S. on visas, green cards, or as naturalized U.S. citizens (numbering 98,969 in 2019, per *U.S. Census Bureau Data*), with retirement savings in SF accounts established prior to relocating to the U.S., and (2) U.S. born or naturalized citizens living and working in Australia (numbering 86,215 in 2016, per *2016 Australian Census*) who are accumulating superannuation benefits.

The U.S. taxes a United States person (USP) based upon that person's worldwide income. Since the scope of the USP definition includes U.S. citizens and resident aliens (green card holders and those satisfying the "substantial presence test"),[43] both categories are exposed to additional U.S. tax and reporting obligations on SF accounts. Compliance with these obligations requires understanding and correct application of the relevant U.S. laws. As there is no U.S. retirement savings plan comparable to superannuation and there is limited guidance on the U.S. tax treatment of these accounts, this creates uncertainty that can lead to incorrect or delinquent reporting, tax deficiencies, and tax penalties and interest. The associated rule complexity and compliance complexity violates an

[28] PBO Budget Explainer, *supra* note 16, at 10-12.
[29] *Contributions to Individual Retirement Arrangements (IRAs)*, IRS Publication 590-A (2022).
[30] SSA.gov, *How is Social Security Financed?*
[31] Ato.gov.au, *How to save more in your Super*.
[32] § 402(b).
[33] IRS, *Topic No. 451, Individual Retirement Arrangements (IRAs)*.
[34] IRS, Publication 590-A (2022), Contributions to Individual Retirement Arrangements (IRAs).
[35] § 402(b)(4).
[36] IRS, Publication 590-B (2022), *Distributions from Individual Retirement Arrangements (IRAs)*; and Publication 575 (2022), *Pension and Annuity Income*.
[37] *Id.*
[38] § 402(b)(2).
[39] *Id.*
[40] IRS, *401(k) Resource Guide - Plan Participants - General Distribution Rules*.
[41] IRS, *Publication 590-A (2022), Contributions to Individual Retirement Arrangements (IRAs)*.
[42] SSA, *What You Need to Know When You Get Retirement or Survivors Benefits*.
[43] § 7701(a)(30)(A) and § 7701(b)(1)(A).

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affected taxpayer's rights, provided in the IRS's *Taxpayer Bill of Rights*, to know what is necessary for tax compliance and to have clear explanations of laws and procedures to pay the amount of tax legally due. They also contravene principles of transparency and simplicity, with the limited guidance creating real costs for taxpayers in compliance burdens.[44]

Two categories of individuals are affected by the currently unsettled state of the law: (1) Australian nationals living in the U.S. on visas, green cards, or as naturalized U.S. citizens and (2) U.S. born or naturalized citizens living and working in Australia.

A. U.S. Disclosure Obligations

A variety of U.S. disclosure obligations are likely to apply to superannuation accounts. For example, a superannuation account is a foreign account and foreign financial asset for Foreign Account Tax Compliance Act (FATCA) and Financial Crimes Enforcement Network reporting purposes, requiring that a USP file a *Report of Foreign Bank and Financial Accounts* (FBAR) for a financial interest in or authority over the account when the aggregate value of their foreign financial accounts exceeds $10,000 at any time during the calendar year reported. A Form 8938 may also be required to be filed to report interests in foreign financial assets with values exceeding certain reporting thresholds. Since the IRS treats SFs as foreign trusts,[45] the grantor trust (GT) rules of sections 671-679 may also apply to SMSFs if members are seen to control and/or own the trust. Contributions to and distributions from SF accounts may also be transactions with a foreign trust requiring disclosure in *Form 3520* and *Form 3520-A*.[46] If an SF is a type of foreign mutual fund, then *Form 8621* disclosure may also be required under the passive foreign investment company (PFIC) rules. There are significant penalties and other consequences associated with non-compliance with these reporting obligations.

Table 2. Disclosure Obligations and Associated Penalties for Noncompliance

IRS Reporting	Required?	Penalties (non-willful compliance)
FBAR	Yes, if the aggregate value of foreign financial accounts > $10,000	$10,000[47]
Form 8938	Yes, if value > specified thresholds (USD $50,000 - $400,000 depending on tax filing status and residency)	$10,000 (or more)[48]
Form 3520	Yes, if there are "transactions with a foreign trust"	Greater of $10,000 or 5% of the gross value of the portion of the trust's assets treated as owned by the USP[49]
Form 3520-A	Yes, if SMSF is a GT	
Form 8621	Maybe, depends on fund structure and underlying assets	Statute of limitations for assessing penalties suspended until filed[50]

If contributions to a SF account, earnings within the account, and distributions from the account constitute foreign income for U.S. tax purposes, such amounts must be declared in *Form 1040* to avoid deficiency assessments and penalties. Compliance with these tax obligations is imperative,

[44] Tax Foundation, *Principles of Sound Tax Policy*.
[45] Reg. § 301.7701-4(a); PLR-124608-14; PLR-139650-14; PLR-139636-14.
[46] It is unclear whether a SF would qualify as a "tax-favored foreign retirement trust" and be exempted under Rev. Proc. 2020-17 from the information reporting requirements of section 6048, due to contribution limits.
[47] IRS, *FATCA Information for Individuals*.
[48] *Id.*
[49] IRS, *Instructions for Form 3520* and *Instructions for Form 3520-A*.
[50] § 6501(c)(8).

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but this is not a simple matter. For example, the SF structure, the identity/capacity of the taxpayer, and application of foreign tax credits (FTCs) can create anomalous outcomes leading to violation of the principle of horizontal equity. If contributions to and earnings within a SF are taxable in the U.S., an FTC may not be claimed by the SF member with respect to taxes paid in Australia by a Large Fund trustee, as they are not the same taxpayer.[51] With SMSFs, each member/trustee has an ascertainable account balance and an equal voting interest in the decisions of the SF. If SMSFs are GTs, a USP who is the GT beneficiary is treated as the trust owner to the extent the beneficiary has made (directly or indirectly) transfers of property to the trust under section 672(f)(5). A USP who holds an SMSF account may thus be treated as the owner of their portion of the fund, exposing them to income reporting and Form 3520-A disclosure. As the USP is treated as having paid any foreign taxes paid by the grantor or the trust on income that the USP is deemed to have received personally, they may claim FTCs.

This anomaly violates the tax policy principles of tax neutrality and creates transactional complexity as affected taxpayers can influence the U.S. tax outcome by structuring their SF accounts in SMSFs instead of Large Funds. While it may appear advantageous for such taxpayers to simply transfer their superannuation balances into SMSFs (and thereby achieve the collateral tax benefit of an FTC), the associated compliance costs can be significant for compliance and reporting obligations in both countries. The SMSF would also need to be appropriately structured under Australian law to ensure compliance with restrictions on the control of entities by non-residents. This is often a costly exercise that violates the principle of vertical equity: it is wealthier taxpayers who may already be structured in SMSFs or who have resources to consult international tax attorneys to roll over their SF accounts from Large Funds into SMSFs.

Disclosing SMSF earnings as income was the approach adopted by PriceWaterhouseCoopers in the original U.S. tax returns filed for taxpayer Dixon (an Australian national resident in the U.S.) in *Dixon v. United States* and the grounds on which the IRS sought to amend its answer to the original Tax Court petition.[52] Ultimately, there was no judicial resolution of the superannuation issues raised, as the amended returns had not been duly filed: Dixon's tax advisor signed amended returns without the required power-of-attorney.[53] Although PwC's approach was technically compliant with the GT attribution rules, how the GT rules apply to SMSFs still requires clarification.

Application of the GT rules to SMSFs with two or more members requires careful review. While SMSF trustees may develop and implement the fund's investment strategy and make investment decisions, they are subject to the same external controls as Large Funds, which restrict their ability to deal with SMSF property and require accountability and annual reporting to the Australian Treasury Office.[54] For example, unlike the general rule for GTs, the ability to make substantial decisions relating to SMSF trust is limited: decisions on whether to distribute income and capital, how much to distribute, and to whom, and who can be trustee are dictated by law rather than being made by the grantor/beneficiary. Further, control under regulation section 1.6038-2 ordinarily requires a more than 50% interest in voting power and assets, but that is arguably absent when a trust with more than one member provides for each trustee/member to have an equal right to vote or otherwise participate in the decisions of the trust. Further, section 672 (a) – (c) requires careful consideration of the facts

[51] IRS.gov, Foreign Tax Credit, § 641; Regs. § 1.642(a)(2)-1.

[52] *Dixon v. United States*, 2:19-cv-14101 (D.N.J. filed June 21, 2019); *Dixon v. Commissioner*, No. 13874-19 (T.C. filed July 25, 2019); *Dixon v. United States*, No. 19-270T (Fed. Cl. 2020); *Dixon v. United States*, 147 Fed. Cl. 469 (2020); *Dixon v. United States*, 158 Fed. Cl. 69 (2022); *Dixon v. United States*, No. 22-1564 (Fed. Cir. 2023), collectively, the "*Dixon Cases*".

[53] *See Dixon v. United States*, No. 22-1564 (Fed. Cir. 2023).

[54] Ato.gov.au, *Self-managed super funds*.

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when members have adverse interests or are related or subordinate to each other, potentially resulting in *no* member having control, or *each* having control. The IRS has not provided guidance on these matters.

The FTC issue discussed above also applies in the context of the different taxing points under each tax regime. Australia taxes the SF trustee on contributions and earnings, but not distributions. The U.S. expressly taxes SF distributions, including (as discussed in IRS Memorandum No. 200604023) death benefit payments. No U.S. tax is payable by a beneficiary on distributions from a foreign GT, if a beneficiary statement is attached to Form 3520 and Form 3520-A. This concession, however, has no effect for USPs with SF accounts when no Australian tax has been paid on distributions, even though Australia would have already taxed the underlying amounts within the fund at two prior taxing points.

B. Limited Guidance

1. The U.S.-Australian Income Tax Treaty

The U.S.-Australian Income Tax Treaty (the Treaty)[55] does not address the U.S. tax treatment of contributions and earnings. The taxation of distributions depends on whether they are considered social security payments, pensions, or annuities, and the classification is unclear. Article 18 allocates the taxing rights for pensions, annuities, and social security payments, as follows:

> (1)… pensions and other similar remuneration paid to an individual who is a resident of one of the Contracting States in consideration of past employment shall be taxable only in that State.
>
> (2) Social Security payments and other public pensions paid by one of the Contracting States to an individual who is a resident of the other Contracting State or a citizen of the United States shall be taxable only in the first-mentioned State.
>
> (3) Annuities paid to an individual who is a resident of one of the Contracting States shall be taxable only in that State.
>
> (4) The term "pensions and other similar remuneration"…. means periodic payments made by reason of retirement or death, in consideration for services rendered, or by way of compensation paid after retirement for injuries received in connection with past employment.
>
> (5) The term "annuities"… means stated sums paid periodically at stated times during life, or during a specified or ascertainable number of years, under an obligation to make the payments in return for adequate and full consideration (other than services rendered or to be rendered).

Article 18 must be read with Article 1 Personal Scope, Section (3), which gives the U.S. authority to tax its citizens under certain provisions of the Treaty as if there were no treaty, regardless of any contrary statement in the Treaty.

[55] *Double Taxation Taxes on Income Convention Between the United States of America and Australia 1983, as amended by the Protocol signed at Canberra on September 27, 2001, Art.4, P 1(a)(iv).*

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> (3) Notwithstanding any provision of this Convention, except paragraph (4) of this Article, a Contracting State may tax its residents and by reason of citizenship may tax its citizens, as if this Convention had not entered into force.
>
> (4) The provisions of paragraph (3) shall not affect:
>
> > (a) the benefits conferred by a Contracting State under paragraph (2) or (6) of Article 18 (Pensions, Annuities, Alimony and Child Support), Article 22 (Relief from Double Taxation), 23 (Non-Discrimination)

Thus, if distributions are classified as pensions or annuity payments to U.S. citizens (even if they are Australian residents), they are also subject to U.S. tax pursuant to Articles 18(1), (3), and 1(3). If such distributions are classified as Social Security payments however, they are not taxable in the U.S., as Article 18(2) is excluded from the reach of Article 1(3) under Article 1(4)(a).

The taxation of distributions depends on whether they are considered social security payments, pensions, or annuities, and the classification is unclear.

The Treaty's Article 23 nondiscrimination clause preventing more burdensome taxation than U.S. resident citizens has limited effect in addressing this outcome due to the U.S.'s right to tax citizens on worldwide income. Because the nondiscrimination clause attempts to limit the U.S. tax on a foreign national to that which the U.S. can impose on a U.S. national where they are in the same circumstances, Article 23 should mean that a U.S. citizen who is resident in Australia cannot be subject to tax more burdensome than that to which an Australian citizen resident in Australia is subject; and conversely, that an Australian citizen resident in the U.S. cannot be subject to tax more burdensome than that to which a U.S. citizen resident in the U.S. is subject. The clause has limited effect because U.S. citizens being subject to tax on worldwide income and Australians being subject to tax based on residency in Australia are not "in the same circumstances."[56] Consequently, there is no violation of Article 23 when the U.S. taxes its citizens on SF distributions.

2. The U.S.-Australian Social Security Agreement

The 2001 Agreement between the Government of the United States of America and the Government of Australia on Social Security (the Totalization Agreement) provides shared coverage of pension payments to those otherwise not entitled due to insufficient qualifying periods of coverage in Australia and in the U.S. or who could not otherwise claim a pension due to non-residency. Article 2(1)(a) of the Totalization Agreement covers U.S. Social Security benefits and Australian welfare payments such as the Age Pension and the Disability Support Pension. Article 2(1)(b) specifically includes "the law concerning the superannuation guarantee" in (ii), but it appears to limit its operation to exempting U.S. employers from the superannuation guarantee for workers subject to U.S. law.

> *[W]hen a worker is subject to U.S. laws and exempt from Australian laws in accordance with Part II [describing the superannuation guarantee], the worker's employer will be exempt from the SG requirements.* Annotation for Article 2(1)(b)(i)

[56] *Farina v. C.I.R.*, T.C. Summ. Op. 2009-23, 2009 WL 416060 (T.C. 2009).

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3. The U.S.-Australia Estate Tax Treaty

Retirement plan benefits are included in the value of the deceased's gross estate for U.S. estate tax purposes under section 2033.[57] The U.S.-Australia Estate Tax Treaty (Australian Treaty Series 1953 No 4, enacted prior to the superannuation laws and the repeal of the Australian Federal estate duty) does not refer to retirement accounts.

III. Recommendations For Taxing Superannuation Accounts

These factors have led tax practitioners either to adopt a treaty-based approach (discussed below) pursuant to which no U.S. tax is paid or alternatively to adopt a more cautious approach which results in double taxation and the nonrecognition of taxes paid in Australia. These divergent approaches create inequity; a lack of neutrality, certainty, and transparency; and the potential for a tax gap as more aggressive taxpayers seek to avoid U.S. taxation while conservative taxpayers pay more tax than may be required. Certain initiatives could address these problems.

A. Extending the FTC Rules to Australian Taxes Paid Within the SF

To ensure uniform tax outcomes between structures, the U.S. should extend the availability of FTCs to Australian taxes paid on contributions to and earnings within the SF for SF accounts held by USPs. This approach is reasonable and tax effective. A similar approach already exists for section 851 mutual fund/regulated investment company (RIC) shareholders who may claim a Foreign Tax Credit for Individuals based on their share of the foreign income taxes paid by those entities. The rationale for the introduction of this approach for RICs—to eliminate unneeded reporting and reduce taxpayer confusion[58]—is equally applicable in the SF context. This approach is fairer and prevents indirect double taxation, since it addresses the misalignment of the taxation of trustees in Australia and the individual member in the U.S. on essentially the same underlying amounts.

To ensure parity between the Australian and U.S. tax systems and ensure that all SF account holders who are USPs are treated equally, this approach requires that affected taxpayers report contributions to superannuation accounts as income for U.S. tax purposes. Affected taxpayers should also report earnings within all SF accounts as income, especially if treated as income within SMSFs under the GT rules. This seems appropriate even though earnings in an SF account could arguably not be includible in gross income as realization and complete dominion over the funds are absent, given the strict regulatory regime governing access to Large Funds.

B. Treating SF Distributions as Social Security Payments or as Roth IRAs

One approach to treatment of SF distributions is to recognize the similarities between superannuation and the FICA/SECA taxes and treat superannuation distributions like Social Security payments. The U.S. taxation of SF distributions depends on the Treaty classification. Ideally, SF distributions would be characterized as equivalent to Social Security payments, in parity with the U.S. system. This treaty-based position would have the effect of exempting superannuation distributions from being taxed in either country. This is a tax efficient outcome as the amounts have previously been taxed in Australia (albeit at the entity level). To subject distributions to further U.S. taxation with no accom-

[57] § 2033.

[58] *Elimination of Country-by-Country Reporting to Shareholders of Foreign Taxes Paid by Regulated Investment Companies*, (Aug 24, 2007).

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panying FTC results in indirect double taxation, an unfair outcome that undermines the intention of the Treaty. It also undermines the goal of maximizing retirement savings for retirees to reduce the future burden on state-funded welfare. If it is determined that superannuation distributions should be classified as Social Security payments, then the rules taxing Social Security would also apply to SF death benefits to ensure consistency and uniformity in the application of the law between each country. Further consideration of this issue by the IRS and Treasury is essential.

Alternatively, the IRS and Treasury could conclude that the similarities between Roth IRAs and SFs are more important, with the result that SF distributions would not be treated as Social Security payments and death benefit payments would be income tax-free when paid to a surviving spouse or to minor, disabled, or dependent adult children in recognition of taxes having been previously paid in Australia.

Table 3. Summary of Recommendations

	Australia (from Table 1)		**Tax Treatment in the U.S.**		**Why?** **Tax Policy Considerations**
Issue:	**Concessional**	**Non-concessional**	**Current**	**Proposed**	
Taxation of contributions	Trustee taxed within the fund	Marginal tax rates (pre-contribution)	Possibly taxable if: • SMSF account • Large funds are classified as non-exempt trusts	• Treat as taxable to achieve parity between Australia superannuation and U.S. Social Security. *Requires clarification as to whether distributions are "social security."* Extension of the FTC for tax paid by Large Fund trustees. *Similar rules exist for mutual funds and RICs, but requires clarification of the application of GT rules for SMSFs.*	• Promotes horizontal equity. • Promotes tax efficiency and neutrality - avoids taxpayers making economic decisions (structuring) merely to achieve collateral tax benefits.
Taxation of earnings within the fund	15% (pre-distribution)	15% (pre-distribution)	Possibly taxable for SMSF accounts under GT rules.	• Extension of the FTC for tax paid by Large Fund trustees. *Requires clarification of the application of GT rules for SMSFs.*	• Promotes horizontal equity. Promotes tax efficiency and neutrality - avoids taxpayers making economic decisions (structuring) merely to achieve collateral tax benefits.
Taxation of distributions / withdrawals	Generally, tax-free if account holder is over age 60.	Generally, tax-free if account holder is over age 60.	Unresolved. Possibly tax free if equivalent to social security, as per *Dixon* arguments.	• Treat as social security for Treaty purposes. *Requires IRS Guidance.*	• Tax efficiency and fairness. • Avoids indirect double taxation. • Maximizing retirement benefits for retirees • Avoiding reliance on welfare. Encourages savings.
Taxation of death benefits	Generally, tax-free if paid to a superannuation dependent	Generally, tax-free if paid to a superannuation dependent	Taxable to beneficiary per IRS.	• Tax as per social security survivor benefits. • Otherwise, treat as tax-free if equivalent to Roth IRA benefits. *Requires IRS guidance.*	• Tax efficiency and fairness. • Consistency and uniformity in the application of the laws for items with similar classification.

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