SUPERANNUATION CHANGES ANNOUNCED IN THE 2016-17 BUDGET AS CHANGED BY AN ANNOUNCEMENT ON 15 SEPTEMBER 2016

By Trevor Nock

Removal of the work test for those aged 65 to 74

This proposal that was announced in the budget has now been withdrawn.

This is very disappointing as it would have allowed many SCOA members to make superannuation contributions in their retirement.

Tax deduction for personal superannuation contributions

From 1 July 2017 all people up to age 65 and to age 75 for those who meet the work test will be able to claim a tax deduction for personal superannuation contributions to a superannuation fund regardless of employment circumstances. Previously, to be able to claim a tax deduction for personal superannuation contributions the person's income from employment was required to be less than 10% of total income. This rule will be removed from 1 July 2017.

Tax deductible personal contributions together with any other concessional contributions (superannuation guarantee and salary sacrifice contributions) cannot exceed the member's concessional contribution cap which, from 1 July 2017 will be $25,000.

The only change to this measure following the 15 September 2016 announcement is that those over age 65 and under age 75 will be required to meet the work test.

Catch-up of concessional contributions

From 1 July 2018 people will be able to make additional concessional contributions where they have not reached their concessional contribution cap in previous years. Access to these unused cap amounts will be limited to those with a superannuation balance of less than $500,000. Amounts are to be carried forward on a rolling basis for a period of five consecutive years, and only unused amounts accrued from 1 July 2018 can be carried forward.

The commencement of this measure has been delayed from what was announced in the budget. Only unused amounts from 1 July 2018 can be carried forward from the 2019/20 financial year.

Increase in the threshold for tax offset for spouse contributions to low income spouse

From 1 July 2017 the threshold for the low income spouse superannuation tax offset will be increased to $37,000. If the spouse has an income of less than $37,000 the other spouse will receive a tax offset of 18% of the amount of superannuation contributions contributed to the spouse's superannuation fund up to a maximum tax offset of $540. For example, superannuation contributions to a spouse's superannuation fund of $3,000 will carry an entitlement to a tax offset of $540 - provided the spouse's income is less than $37,000.

No change to this measure.

A cap of $1.6 million to be placed on the amount that can be transferred from the accumulation phase to the pension phase in a superannuation fund

From 1 July 2017 the Government proposes to introduce a cap of $1.6 million that can be transferred from the accumulation phase to the pension phase of a member's superannuation account. After the transfer, subsequent earnings on the assets held in the pension phase will not be restricted.

Where a superannuation fund member has assets greater than $1.6 million in the pension phase before 1 July 2017, they will be required to transfer the excess above $1.6 million back to the accumulation phase.

Tax on amounts that are transferred to the pension phase in excess of the $1.6 million cap (including earnings on those excess transferred amounts) will be applied at the top marginal tax rate plus Medicare levy.

The amount of cap space remaining for a member who makes more than one transfer to the pension phase will be determined by apportionment, having regard to draw downs and earnings.

Commensurate treatment for members of defined benefit schemes will be achieved through changes to the tax arrangements for pension amounts over $100,000 from 1 July 2017.

Accumulation phase

Assets in the accumulation phase consist of contributions made to the superannuation fund and earnings on those assets. Tax at 15% is applied to the earnings on those assets. Once a member has reached preservation age and retired or reached age 65 they can make withdrawals.

Pension phase

Once a member has reached preservation age and retired or reached age 65 they can transfer assets from the accumulation phase to the pension phase. Earnings on assets in the pension phase are tax free. Regular withdrawals at or above a set minimum amount are required to be made from the pension phase.

Application to CSS and PSS Members

The transfer balance cap of $1.6M will apply to defined benefit pensions paid to CSS and PSS members. The transfer balance cap for pensions is $100,000 per annum ($1.6M ÷ 16)

Where there is a commutable pension or the pension is backed by an amount in the pension phase of a superannuation fund, the pension needs to be commuted down to a pension of $100,000 per annum or the amount in the pension phase needs to be reduced down to $1.6M.

If the pension is not commutable then there is an adjustment to the tax levied on that pension. The funded component of the pension is applied against the $100,000 per annum cap first. Therefore, for example, if a PSS member has a PSS pension of $130,000 per annum and $50,000 was funded and $80,000 was unfunded the following tax provisions would apply.

> $50,000 tax component would be tax free.
>
> $80,000 untaxed component would be subject to a tax offset of $5,000.

As $30,000 of the unfunded component exceeds the $100,000 cap, $3,000 of tax offset is lost.

The following applies where a CSS member has a private superannuation fund or a SMSF and a CSS pension and the balance of the superannuation fund is $1.2M and the unfunded CSS pension is $60,000 per annum. The member will be required to reduce the $1.2M down to $640,000 by transferring $560,000 out of the pension phase of the superannuation fund so that the amount in the pension phase and the CSS pension will equal the transfer balance cap ($640,000 + $60,000 x 16)=$1,6000,000)).

Action can be taken before 1 July 2017 to take the excess over $1.6 million ($560,000 in the example above) as a commutation lump sum or transfer amount back to the accumulation phase of the superannuation fund. If action is not taken before 1 July 2017, the ATO will require the amount excess to $1.6 million and any interest on the excess to be taken as a commutation lump sum. Tax will be levied on the interest accrued on the excess from 1 July 2017.

The transfer balance cap will be indexed to CPI.

Comment

The transfer balance cap does not differentiate between unfunded (untaxed) benefits and funded (taxed) benefits.

The amount applying to a taxed benefit has already been taxed and therefore is a lower amount when compared to an untaxed benefit, which is higher because it has not yet been taxed.

These differences were taken into account when calculating the reasonable benefit limits (RBLs) that applied before 2007. Unfunded benefits applying against the RBLs were reduced by 15% to take into account that tax had not been levied against those benefits.

By comparing a $100,000 funded defined benefit pension to an unfunded defined benefit pension the unfunded defined benefit pension should increase to $117,648 before the 10% tax offset is lost. Alternatively the amount for unfunded (untaxed) benefits should be $1,882,353 ($1,600,000 grossed up by 15%) instead of $1,600,000. This would make the calculation of the transfer balance cap equitable between taxed and untaxed benefits.

Cap on non-concessional superannuation contributions

This measure has been changed substantially. The measure is now as follows.

From 1 July 2017, the Government will lower the annual non–concessional contributions cap to $100,000 and will introduce a new constraint such that individuals with a balance of more than $1.6 million will no longer be eligible to make non–concessional contributions. As is currently the case, individuals under age 65 will be eligible to bring forward 3 years of non–concessional contributions.

The $1.6 million eligibility threshold will be based on an individual’s balance as at 30 June the previous year. This means if the individual’s balance at the start of the financial year (the contribution year) is more than $1.6 million they will not be able to make any further non–concessional contributions. Individuals with balances close to $1.6 million will only be able to access the number of years of bring forward to take their balance up to $1.6 million.

The $1.6million will be indexed to CPI (inflation) while the $100,000 cap will be indexed to average weekly earnings (wages).

Transitional arrangements will apply. If an individual has not fully used their non–concessional bring forward before 1 July 2017, the remaining bring forward amount will be reassessed on 1 July 2017 to reflect the new annual caps.

Individuals aged between 65 and 74will be eligible to make annual non–concessional contributions of $100,000 if they meet the work test (that is they work 40 hours within a 30 day period each income year). As per current arrangements, they will not be able to access the three year bring forward of contributions.

Low income superannuation tax offset

From 1 July 2017 the Government will introduce a Low Income Superannuation Tax Offset (LISTO) to reduce tax on superannuation contributions for low income earners.

The LISTO will provide a non-refundable tax offset to superannuation funds, based on the tax paid on concessional contributions made on behalf of low income earners, up to a cap of $500. The LISTO will apply to members with adjusted taxable incomes of up to $37,000.

This measure effectively reintroduces the previous Government's Low Income Superannuation Contribution (LISC) that was abolished by the current Government.

No change to this measure.

Concessional contribution limits and cap

From 1 July 2017 the Government will lower the concessional contribution cap to $25,000 for all superannuation fund members.

The threshold for high income earners will reduce from $300,000 to $250,000. A contribution tax of 30% will be applied to concessional contributions made in respect of those with incomes greater than $250,000.

From 1 July 2017, the Government will include notional (estimated) and actual employer contributions in the concessional contribution cap for members of unfunded defined benefit schemes. How this will work is unclear.

No change to this measure.

Transition to retirement pensions

From 1 July 2017 transition to retirement pensions will be required to be paid out of the accumulation phase, where fund earnings are taxed at 15%, instead of the pension phase where fund earnings are tax free.

No change to this measure.

Removal of the anti-detriment provisions for death benefit lump sums

These provisions allows a refund of contribution tax to be paid back to the superannuation fund and then on to the lump sum beneficiary where the beneficiary (spouse or child) is a dependant of a deceased account holder. These provisions were dependent upon superannuation funds making an application to the ATO for a refund of contribution tax paid. Not all superannuation funds were inclined to make such an application and as a consequence this provision was applied inconsistently across superannuation funds. From 1 July 2017 the Government will remove this provision.

Deferred annuities

The Government has also confirmed that it will remove tax barriers to the development of new retirement income products by extending the tax exemption on earnings in the retirement phase to products such as deferred lifetime annuities and group self-annuitisation products.

These products can provide more flexibility and choice for retirees, and help them to better manage consumption and risk in retirement.

No change to this measure.