With a 1 July 2017 start date, there is not much time to adjust your Superannuation strategies

What the recent Super changes mean for you…

The superannuation changes announced in the 2016 Federal Budget and recently legislated are the most significant of the past 10 years and in many respects represents a change of thinking for fund members.

It is important that you understand how the recent super changes may impact you and your retirement benefits. Affected persons need to consider ***acting now*** to ensure the impacts are reduced and/or your benefits maximised.

A brief summary of the key changes, which come into effect on 1 July 2017, are outlined below.

$1.6m transfer balance cap to retirement phase

From 1 July 2017, super fund members will be limited to a $1.6 million transfer balance cap to fund retirement phase pensions (eg, account based pensions). Amounts in excess of the lifetime cap will not attract the tax exemption for earnings from assets in retirement phase and will be required to be held in the accumulation phase and taxed at 15%. These changes are the most complex of the Government's superannuation package.

<u>Key planning issues:</u>

- *For people with existing superannuation income streams, the total value of an individual's superannuation interests supporting income streams at 30 June 2017 will count towards their $1.6 million transfer balance cap.*
- *The cap will operate on the basis of "credits" counting to the cap and "debits" removing value from the cap (much like a bank account or a general ledger).*
- *Credits will be created by:*
  - *the value of super interest supporting income streams on 30 June 2017,*
  - *commencement of new superannuation income streams from 1 July 2017 onwards,*
  - *the value of reversionary income streams when an individual becomes entitled to them, and notional earnings accruing to excess transfer balance amounts.*
- *Debits will be created by:*
  - *commutations of superannuation income streams (including partial commutations),*
  - *structured settlement payments contributed to superannuation, and*
  - *certain payments arising from family law splits, fraudulent or void transactions.*

- *Partial commutations will not count towards a person's minimum drawdown requirements under the new rules (but do for 2016/17 which represents an opportunity for pensioners under age 60).*
- *Investment gains and losses do not alter the transfer balance cap. Income stream payments do not change the transfer balance cap either.*
- *Reversionary pensions will count towards the cap, but taxpayers will have a 12 month period to deal with the reversionary pension before a credit arises and counts towards their cap. This deferral also applies to individuals who are receiving a reversionary pension on 30 June 2017.*
- *Non-reversionary pensions and new death benefit pensions count towards the beneficiary's cap on the date that they begin being paid to the beneficiary.*
- *Breaches of the cap will require the excess amounts to be removed which will necessitate the commutation of the relevant income stream which has exceeded the cap.*
- *The ATO will be able to issue a commutation notice setting out the amount an income stream must be reduced by. If the commutation notice is not complied with, then the entire income stream will not be eligible for the tax exemption for earnings from assets supporting an income.*
- *Excess amounts will also attract "notional earnings" which count towards the transfer balance cap. Notional earnings are charged at the 90 day bank accepted bill rate plus seven per cent.*
- *An excess transfer balance tax of 15 per cent will apply to the notional earnings. After receiving one excess transfer tax determination, a tax rate of 30 per cent applies to any excess transfer balance tax assessments the individual receives in a subsequent financial year.*
- *The transfer balance cap will be indexed in line with the Consumer Price Index and increased in $100,000 tranches.*
- *Individual's may only access a proportion of the newly indexed amount consistent with the unused proportion of their transfer balance cap, rather than the full $100,000 increase when it is available.*
- *A child receiving a superannuation death benefit income stream will have a modified transfer balance cap which is linked to their deceased parent's cap.*
    - *If a child is receiving superannuation income streams as a child recipient when these amendments begin to apply, the child's transfer balance cap is $1.6 million.*
    - *If the deceased parent did not have a transfer balance account at the time of their death (i.e. they had not yet entered retirement phase), and they died on or after 1 July 2017, the child's cap is their proportionate share of the deceased's superannuation interests multiplied by the $1.6 million transfer balance cap.*
    - *If the deceased person did have a transfer balance account, the child beneficiary is entitled to their portion of the deceased's superannuation interests that were in the retirement phase.*

- *"Capped defined benefit income streams" have special rules for the transfer balance cap recognising their non-commutable nature. These modifications apply to lifetime pensions/annuities, life expectancy pensions/annuities and market-linked pensions/annuities.*
    - *Where the value of a capped defined benefit income stream exceeds the transfer balance cap, it will not give arise to excess transfer balance tax but instead will attract additional income tax on the income stream.*
- *Approaching 1 July 2017, people may want to restructure their asset holdings to be in a position to maximise the $1.6 million cap especially between spouses.*

ACTION: If you are over, near or have the potential to be impacted by the $1.6 million cap, it is important that you contact me. I can advise you on options that may be available to reduce the impact of this change. Not proactively restructuring your fund before 30 June 2017 can result in tax penalties.

Non-concessional contribution cap reduction

The Government has abandoned its proposed $500,000 lifetime cap on non-concessional contributions (NCC) and instead will reduce the annual NCC to $100,000 per annum and restrict access to taxpayers with a total superannuation balance of under $1.6 million.

Key planning issues:

- The $180,000 annual NCC cap for 2016-17 is available to people who satisfy the conditions for making a NCC under the current rules.
- The $540,000 bring forward rule will apply for the remainder of 2016-17 income year for those eligible.
- If the bring forward provision is triggered in 2016-17 but the full $540,000 amount is not used, then the bring forward cap available in 2017-18 and 2018-19 will be reduced.
- Post 1 July 2017 taxpayers with over $1.6 million in superannuation will not be able to make NCCs to superannuation.
- Also, taxpayers who are approaching a balance of $1.6 million will have their ability to use the bring forward rule reduced. Where a superannuation balance is between $1.4 million and $1.5 million the bring forward rule will be limited to a maximum of $200,000.
- In addition, where a superannuation balance is between $1.5 million and $1.6 million the bring forward rule will be limited to a maximum of $100,000.

ACTION: At present, a significantly higher amount of up to $540,000 could be contributed to superannuation as a non-concessional contribution. Given that superannuation is still a very attractive vehicle to hold your retirement assets, it is important that you do not miss out on the potential to make larger contributions to superannuation before the 1 July 2017 deadline.

Various tax and administrative issues need to be considered, including being aware of the amount of past contributions, hence the importance of obtaining advice early on this important change.

Concessional contribution cap reduction

The concessional contribution cap will reduce to $25,000 per annum for all taxpayers from 1 July 2017.

Key planning issues:

- Fund members should look to maximise the current contribution caps for 2016-17 which are:
    - $30,000 for people aged under 49 on 30 June 2016, and
    - $35,000 for people aged 49 and over on 30 June 2016.
- Caution should be taken for reserving strategies executed in June 2017 as the 2017-18 cap restricts amounts reserved in June 2017 to a maximum of $25,000.
- The concessional cap is indexed in $2,500 increments in line with Average Weekly Ordinary Time Earnings.

ACTION: If possible bring forward any concessional contributions as this may enhance your overall financial position. For SMSFs, consider using contributions reserving strategies to potentially "double up" on your concessional contributions in 2016/17. This, of course, is subject to your personal situation and tax rate.

Removal of the segregated method in certain circumstances for SMSFs

This was an unexpected element of the Government's superannuation package which was introduced as an integrity measure for the $1.6 million transfer balance cap. Its intent is to stop taxpayers cycling assets between segregated tax exempt assets in retirement phase and the 15% taxed accumulation phase where they have assets in excess of $1.6 million in super.

Key planning issues:

- Taxpayers with in excess of $1.6 million in superannuation will be required to use the unsegregated method to calculate the tax their fund must pay on earnings when they have assets in retirement phase and assets in excess of $1.6 million.

Loss of tax free status for Transition to Retirement Income Streams (TRIS)

This change will see that tax-exempt treatment of earnings on assets supporting a transition to retirement income stream (TRIS) cease as of 30 June 2016. From 1 July 2017, fund members can still start (or maintain a pre-existing TRIS) but without the tax-exempt treatment for earnings.

Key planning issues:

- There will be no grandfathered treatment for existing TRIS.
- There will be tightening of tax rules around receiving regular lump sum payments from 2017/18
- SMSF members with existing TRIS should consider the impact of their assets supporting a TRIS losing the tax exemption from 1 July 2017 on their SMSF's tax position.
- This may prompt some fund members to realise taxable capital gains in the 2016-17 income year to maximise the benefits of their current TRIS arrangements or seek CGT relief as detailed below.

ACTION: If you have a Transition to Retirement Income Stream, please contact me to discuss the impact of the effectiveness of this strategy after 1 July 2017.

CGT relief arrangements for asset transfers

The Government has allowed CGT relief for assets that need to be transferred from retirement phase to accumulation phase due to the $1.6 million transfer cap and changes to TRIS coming into effect.

The CGT relief has been made available to avoid:

- The unintended consequences of tax applying to capital gains which have accrued on assets held or attributable to the tax exempt retirement phase; and
- The impact of the transaction costs of selling down and repurchasing assets to avoid capital gains tax. SMSFs may choose to reset the cost base of the relevant assets to the market value at the time the asset ceases to be a current pension assets or as at 30 June 2017, depending on whether the fund uses the segregated or proportionate (unsegregated) method for the calculation of tax exempt entitlements.

Key planning issues:

- The CGT relief arrangements will allow funds to reset the cost base on CGT assets that are moved or reapportioned from the retirement phase to the accumulation phase from 9 November 2016 until prior to 30 June 2017.
- This will ensure when the assets are sold, only tax is paid on capital gains accruing after 1 July 2017.
- An irrevocable election is to be made in an approved form before the date the fund lodges the 2016/17 income tax return.

ACTION: Determine the value of any cost base reset on an asset-by-asset basis. This will depend on a number of factors and whether the asset has been held on a segregated or unsegregated basis for tax purposes. Any action taken during the period from 9 November 2016 to 30 June 2017 can help (or hinder) your future tax position so it’s important to seek advice in this area now.

Other changes of note…

- The introduction of a Low Income Superannuation Tax Offset, to ensure those on lower incomes (ie. taxable income up to $37,000) receive a refund of contributions tax on superannuation.
- Those eligible for the spouse contribution tax offset will extend to those whose recipient spouses earn up to $40,000.
- The requirement that an individual must earn less than 10 percent of their income to be able to claim a deduction for personal superannuation contributions will be removed. This should provide additional tax deduction opportunities for many people.
- The threshold at which higher income earners pay additional contributions tax (Division 293) will be lowered from $300,000 to $250,000. This change means higher income earners will pay more tax on their concessional superannuation contributions.
- The abolition of the anti-detriment rule which effectively allowed many superannuation funds to claim a tax deduction for a portion of the death benefits paid to eligible dependants. This may impact on SMSFs which have undertaken a strategy to fund this type of payment. Such arrangements need to be carefully unwound taking into account various taxation and contribution issues.
- Opportunity, from 1 July 2018, to make “catch up” concessional contributions.

ACTION: If you are in a scenario where the above may apply, please check with your superannuation fund or myself about the impact on you.

Conclusion

Whilst I have attempted to summarise the key changes, as you could appreciate, each person has different circumstances and it's not possible to advise on the impact of the changes without a consultation with you.

Please don't hesitate to contact me to discuss these important changes.

Yours sincerely,

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