



Budget 2016



Superannuation Reform:

Introducing a \$1.6 million transfer balance cap

The Government will introduce a \$1.6 million cap on the total amount of superannuation savings that can be transferred from a concessional-tax 'accumulation account' to a tax-free 'retirement account'. This will better target tax concessions to ensure the superannuation system is sustainable, and improve confidence in the system by reducing the extent that superannuation is used for tax minimisation and estate planning.

The issue

Superannuation tax concessions are intended to encourage people to save for their retirement. They are not intended to provide people with the opportunity for tax minimisation or for estate planning.

As the earnings from retirement phase superannuation accounts are tax-free they are a

very desirable investment choice for individuals.

Limiting the amount that can be transferred into a tax-free retirement account will make the superannuation system more fiscally sustainable and increase confidence that the settings are consistent with the objective of superannuation.

The details

From 1 July 2017, the Government will introduce a \$1.6 million cap on the total amount of superannuation that can be transferred into a tax-free retirement account.

- Like the Age Pension, the cap will index in line with the consumer price index. The transfer balance cap will increase in \$100,000 increments.
- Superannuation savings accumulated in excess of the cap can remain in an accumulation superannuation account, where the earnings will be taxed at 15 per cent.
- A proportionate method which measures the percentage of the cap previously utilised will determine how much cap space an individual has available at any single point in time.
 - For example, if an individual has previously used up 75 per cent of their cap they will have access to 25 per cent of the current (indexed) cap.
- Subsequent fluctuations in retirement accounts due to earnings growth or pension payments are not considered when calculating cap space.

- Following consultation, the Government commits to reviewing the impact of the transfer balance cap should there be a macroeconomic shock that substantially affects retirement incomes. The review would draw on advice from the Council of Financial Regulators and on actuarial advice to inform what response, if any, may be required.

Consequences for breach

Individuals who breach the cap will be required to remove the excess capital from their retirement phase account and will be liable to pay tax on the notional earnings attributable to the excess capital. The amount removed from the retirement phase can be transferred into an accumulation account, where the earnings will be concessional taxed at 15 per cent, or withdrawn from superannuation.

Those individuals already in retirement as at 1 July 2017 with balances in excess of \$1.6 million will need to either:

- transfer the excess back into an accumulation superannuation account; or
- withdraw the excess amount from their superannuation.

Transitional arrangements will apply for existing account holders.

Individuals can also apply to the Commissioner of Taxation to replenish their transfer balance cap space for anomalous situations that cause their retirement balance to be depleted, such as fraud, bankruptcy or family law splits.

Where a fund moves an asset back to an accumulation account to comply with the introduction of the transfer balance cap before 1 July 2017, the fund will have the option of resetting that asset's cost base to its current market value.

This will ensure that tax will not be applied to gains that accrued while the asset supported a retirement phase interest.

Where an asset is already partially supporting an accumulation account, the fund will have a capital gains tax liability on the non-exempt proportion of the unrealised gains. The liability can be paid immediately or deferred until the asset is sold.

Impact

Very few people will be affected by this proposal. The average superannuation balance for a 60-year old Australian nearing retirement is \$240,000 and less than one per cent of fund members will be affected by the balance cap.

The details of the broadly commensurate treatment for members of defined benefit schemes are in Superannuation Fact Sheet 5.

Budget impact

The measure is estimated to improve the underlying cash balance by \$1.8 billion over the forward estimates.

Cameo - Jason

Jason is 60 and plans to retire during the 2017-18 financial year. Jason expects he will have an accumulated superannuation balance of less than \$1.6 million. This measure does not affect Jason.

Cameo - Agnes

Agnes, 62, retires on 1 November 2017. Her accumulated superannuation balance is \$2 million.

Agnes can transfer \$1.6 million into a retirement income account. The remaining \$400,000 can

remain in an accumulation account where earnings will be taxed at 15 per cent. Alternatively, Agnes may choose to remove this excess amount from superannuation.

While Agnes will not have the ability to make additional contributions into her retirement account, her balance will be allowed to fluctuate due to earnings growth or drawdown of pension payments.

\$1.6 million transfer balance cap

When does the measure start?

- The \$1.6 million transfer balance cap will commence on 1 July 2017.

Is the \$1.6 million transfer balance cap retrospective?

- No. The Government is simply limiting the amount that benefits from the tax-free retirement phase from 1 July 2017.
- Earnings in retirement phase accounts will remain tax-free.
- By the time the new rules apply, individuals who have retirement balances in excess of the transfer balance cap will have had time to transfer any excess into the concessional accumulation phase, where earnings are taxed at 15 per cent, or out of the superannuation system.

Can I make more than one transfer?

- Yes, individuals will be able to make transfers in the retirement phase as long as they have available cap space.
- The amount of the cap space an individual has available will be determined by the proportionate method which measures the percentage of the cap previously utilised.

How many people will this affect?

- It will affect less than 1 per cent of Australians with a superannuation account.
- The average superannuation balance of a 60-year old Australian nearing retirement is \$240,000.

What if I have more than one superannuation retirement account?

Is it \$1.6 million per account?

- No, the cap applies to the total amount of superannuation that has been transferred into the retirement phase, it does not matter how many accounts these balances are held in.
- Similarly, for individuals already in retirement prior to 1 July 2017, the cap applies to the total amount held in the retirement phase, it does not matter how many accounts these balances are held in.

What sort of income and living standards will I have with a \$1.6 million balance in retirement?

- A balance of \$1.6 million is approximately twice the level of assets at which a single homeowner currently loses entitlement to the Age Pension, and almost three times the 'comfortable standard' of the Association of Superannuation Funds of Australia.

Does the cap limit how much I can hold in my retirement phase account?

What happens if my retirement account grows in excess of \$1.6 million?

- The cap only limits the amount you can transfer into a retirement phase account it does not apply to the balance on that account.
- Your balance can grow above \$1.6 million in your retirement phase account. The cap does not apply to this subsequent growth.

Once my retirement phase account balance falls below \$1.6 million, can I transfer more?

- An individual can transfer more into a retirement phase account only if they have not previously exhausted their cap. The amount of the cap space an individual has available will be determined by the proportionate method which measures the percentage of the cap previously utilised.
- If, for example, an individual transfers the full \$1.6 million into a retirement phase account which subsequently decreases the individual will not be able to transfer any more into the retirement phase as they have utilised 100 per cent of their cap space.
- If an individual transfers \$800,000 into a retirement phase account, they will have utilised 50 per cent of the cap space. If the cap is later indexed to, for example, \$1.7 million, they will be able to transfer an additional 50 per cent of the indexed cap, being \$850,000.

What happens if I make transfers in excess of the cap after 1 July 2017?

- If an individual transfers amounts into a retirement phase account in excess of the cap, they will be required to remove the excess (including notional earnings on the excess capital). If they choose not to, their fund will be required to remove the excess on their behalf.
- These amounts can be transferred back into an accumulation account, where the earnings on the excess will be taxed concessional at 15 per cent. Alternatively, the excess can be withdrawn from superannuation.
- For a first breach, individuals will be subject to a 15 per cent tax on the notional earnings.

What happens if I am already retired before 1 July 2017 and have a retirement phase balance in excess of \$1.6 million?

- Individuals already in retirement with retirement phase balances in excess of the cap at 30 June 2017 will be required to either:
 - withdraw these excess amounts from superannuation; or
 - transfer these excess amounts back into an accumulation account.
- The earnings on funds in an accumulation account will be taxed at the 15 per cent concessional tax rate.
- Transitional arrangements will apply for those above \$1.6 million but at or below \$1.7 million – individuals will have 6 months from 1 July 2017 to remedy the breach. If they comply, no further penalty is applicable.
- Those who do not remedy the breach or who have balances above \$1.7 million on 30 June 2017 will be subject to the consequences of their fund removing the excess and a tax on notional earnings on the excess capital.

What if I retired before 1 July 2017 and transferred less than \$1.6 million at that time, but my balance has grown to \$2 million through investment returns?

- You will still need to comply with the cap. If your balance on 30 June 2017 is in excess of \$1.6 million, you will need to remove the excess amount from your retirement account.

How will this cap apply to defined benefit pensions?

- Different arrangements involving changes to the taxation of defined benefit pension payments will be adopted to achieve a broadly commensurate taxation outcome to that of the transfer balance cap.
- Defined benefit pensions will not be required to be commuted and rolled-back if they are valued at over \$1.6 million. Rather, defined benefit pension payments over \$100,000 per annum will be subject to additional taxation to broadly replicate the effect of the \$1.6 million transfer balance cap.

How will this cap apply to non-commutable pensions (commenced prior to 1 July 2017)?

- Non-commutable pensions that commenced prior to 1 July 2017 will be treated the same as defined benefit pensions.

How will this cap apply to non-defined benefit, non-account-based income streams (started after 1 July 2017)?

- Products such as lifetime annuities, market-linked pensions and annuities and term/life expectancy pensions and annuities will be valued using their purchase price.

How will this cap apply to future 'innovative' income stream products?

- These products will be valued using their purchase price.
- If a product is purchased with instalments during the accumulation phase or deferred from the point of purchase, it will be valued using an existing method requiring actuarial certification.
- Collective defined contribution scheme pensions will be valued at the amount of the collective pool of fund assets attributed to the member on the day the pension commences and certified by an actuary.

Do transition to retirement income streams count towards the transfer balance cap?

- No. As transition to retirement income streams (TRIS) will no longer receive an earnings tax exemption from 1 July 2017 they do not count towards the transfer balance cap.

Can I still split my retirement phase interests to purchase or diversify my retirement income streams?

- Yes. Once you have transferred your superannuation income streams to the retirement phase, they are not counted again towards your transfer balance cap.
- To achieve this outcome, your transfer balance account will receive a 'debit' equal to the value of the amount commuted. This amount, plus any unused cap space, may then be used to purchase a new income stream or retirement product.
- To ensure the integrity of this approach, you will no longer be able to use partial commutations to satisfy minimum drawdown requirements.
- If you choose to commute your income streams (either in part or in full) you will receive a debit equal to the value of the commutation.

Do I need to pay tax on income from my retirement account? Or on the amounts that I withdraw from my accumulation phase account?

- No. The Government has not changed the taxation treatment of amounts drawn down from superannuation accumulation accounts by people who have reached their preservation age. Superannuation benefits paid, either as an income stream or as a lump sum, from a funded source (that is, one in which taxes have been paid on contributions and earnings such as in an accumulation scheme or a funded Defined Benefit scheme), are generally tax-free for people aged 60 and over.
- The earnings on amounts in an accumulation phase account are taxed at the concessional 15 per cent tax rate. Withdrawn funds are not taxed, providing the individual has reached age 60. There are no minimum (or maximum) drawdown requirements from accumulation accounts.

Will the \$1.6 million transfer balance cap be indexed?

- Yes. The cap will index in \$100,000 increments in line with the consumer price index, just as the Age Pension assets threshold does.

Do structured settlements or personal injury payouts count towards the cap?

- These amounts will not count towards an individual's transfer balance cap. This will ensure that individuals can continue to access these arrangements which support them in meeting their healthcare and living costs.

For couples where one spouse either does not have a superannuation account or has a low balance in their account/s can they have a joint \$3.2 million cap?

- The transfer balance cap is an individual cap. Each individual can transfer \$1.6 million into their retirement phase account/s from their accumulation account/s.
- An individual with more than \$1.6 million in the retirement phase will need to either transfer the excess to an accumulation account where earnings will be taxed, or withdraw the excess from the superannuation system. Subject to the contribution caps, excess amounts withdrawn could be contributed to their spouse's account.
- In the superannuation system, and most areas of tax, people are taxed and treated as individuals not as families or households.