BIGGEST SUPER CHANGES IN TEN YEARS

EFFECTIVE DATE: All but one of the changes come into effect on 1 July 2017. We will need to act fast together to transition into the new rule.

COMMENTARY ON CHANGES

There are some common misconception with the changes.

- There is no change to the taxation of super benefits. The changes are to the taxation of the superfund itself.

- There is no limit on how much you can have in super. There are contribution limitations, and there is now a limit on how much can be transferred to the pension phase, but there is no limit on how much you can have in super.

  All these new rules say is that if you have more than $1.6 million in super, the excess needs to stay in the so-called accumulation phase. Being in an accumulation account, it will be subject to the standard 15% tax rate in super, or 10% on capital gains where the asset has been held for at least 12 months.

- You need to be aware there are two $1.6 million caps which does add to the confusion. There is a $1.6 million transfer balance cap which effects the amount that can be in pension phase, and a $1.6 million non-concessional contribution cap which does not allow any more non-concessional contributions if a member's super balance exceeds $1.6 million.

SUMMARY OF CHANGES AND STRATEGIES/ACTIONS TO CONSIDER

1 JULY 2017

- Concessional contribution cap reduced from $35,000 (if 49 and over) and $30,000 (if under 49) to $25,000 for all ages.

  Strategy/Action

  Maximise concessional contributions prior to 30 June 2017.

  $35,000 (49 and over), or

  $30,000 (under 49)

- Non-concessional contribution cap reduced from $180,000 to $100,000. There are transitional rules regarding the three year bring forward provisions.

  The three year bring forward amounts have correspondingly been reduced from $540,000 to $300,000.

  Please note the three year bring forward is only available to those under 65.

Strategy/Action

Maximise non-concessional contributions of potentially up to three times the $180,000 cap using the bring forward provisions prior to 30 June 2017.

If you have already triggered the three year bring forward provisions prior to 30 June 2016 we will need to check how much you can contribute prior to 30 June 2017.

If you don't have the cash but you have assets in personal names it may be worth selling or transferring these assets in-specie into super to take advantage of this contribution window. You will need to be careful as this may trigger CGT and/or stamp duty. For those with balances over $1.6 million this will be the last opportunity to make such contributions.

- Super balances in the tax exempt pension phase will be limited to $1.6 million per member. This is known as the Transfer Balance Cap. Super balances in excess of this amount will need to be rolled back into accumulation phase or withdrawn from super altogether.

  Balances over and above the $1.6 million transfer limit will be treated as accumulation balances and earnings will be taxed at 15 per cent.

Strategy/Action

Re-balancing is for a couple to ensure their super balances are as even as possible. For example where one spouse has a balance in excess of $1.6 million and the other spouse has a lower than $1.6 million balance it may be possible to arrange for the higher balanced spouse to withdraw and re-contribute for their spouse. Please note, available contributions caps and eligibility to withdraw and contribute must be observed.

If after attempting to rebalance one or more members still have a balance over $1.6 million than as stated before the excess will need to be rolled back to the accumulation phase ***or*** *withdrawn entirely from super. Rolling back the excess to the accumulation phase is likely to be the best option, rather than withdrawing and investing outside of superannuation. This will depend on your personal circumstances, in particular the type of investment and the level of the member's personal taxable income.*

For those with over $1.6 million balances the next step will be to think about which assets they leave in pension phase and which assets they roll back to the accumulation phase.

Some are arguing it makes sense to hold high growth assets, such as shares and property in the pension account where there is no limit on how much the value of the pension can grow beyond $1.6 million. The challenge will be making sure the pension account has enough liquidity to make the minimum pension requirement each year.

Strategically it may be best to set up a second superfund before 30 June 2017, and rolling over the high growth assets up to $1.6 million into a new fund and *keeping the balance in the original fund. The new fund will be able to grow to any number once the cap has been set.*

The high dividend yielding "boring shares" like Telstra or cash and term deposits may be best held in the accumulation account.

One of the major benefits which has received little attention is that the minimum pension withdrawal amount will now only be based on $1.6 million per member, meaning those members with very high balances will not have to work out what they are going to do with un-needed large pension withdrawals. Indeed this previously un-needed large amount can now be re-invested in the accumulation account of the member within the superannuation fund.

- Super balances supporting a Transition to Retirement Income Stream (TRIS) will no longer be tax exempt.

Strategy/Action

A TRIS is not limited to the $1.6 million cap as the cap only applies to ABPs so in some circumstances it may be a very beneficial option. Those not in TRIS should consider starting one if they are eligible.

TRIS's can either continue or roll-back to accumulation phase. One of the key benefits of having a TRIS in place prior to 30 June 2017 (even if only for a few months) will be the ability to reset your cost base for CGT purposes on 30 June 2017.

Those in TRIS should also consider whether they are eligible to convert to a full accounts based pension (ABP). They will need to meet a "condition of release" which if the member is over 60 involves ceasing an employment arrangement. This could involve quitting one part-time job and retaining a second part-time job.

- Super members with total super balances exceeding $1.6 million will no longer be able to make non-concessional contributions. They will however be able to make small business CGT contributions on sale of a small business.

Strategy/Action

Again maximise non-concessional contributions prior to 30 June 2017 as the $1.6 million non-concessional cap does not take effect until 1 July 2017.

Ideally, any small business CGT contribution should be made after any other contribution, especially where the small business CGT contribution will push account balances over the $1.6 million cap.

- The 10% employment income rule for deductibility of personal concessional contributions will be abolished. All individuals regardless of source of income will be eligible to claim a personal superannuation deduction.

Strategy/Action

The abolition of the 10% rule may make salary sacrificing super contributions redundant. Employees will be able to plan for and make top-up contributions at the end of the year. Salary sacrificing may however be still attractive as a forced saving throughout the year and can result in the tax benefit being received throughout the year rather than waiting until the end.

This change will be very beneficial for those with changed circumstances throughout the year. For example someone on a salary for half the year who then becomes a business owner for the second half would previously had not been eligible for a personal deduction.

Individuals with non SMSF super accounts wishing to claim a personal deduction must realise there is extra paperwork involved and it is their obligation to make sure this is completed prior to lodgement of their tax return and prior to the super contribution being withdrawn or rolled-over.

- The income threshold at which additional super contributions tax applies will be reduced from $300,000 to $250,000.

- The work test (a member must work for at least 40 hours in a 30 day period to contribute) for those aged between 65 and 74 has not been abolished as had previously been announced.

- Transitional CGT relief available

  Very broadly the CGT relief arrangements will allow funds to reset the cost base on CGT assets that are moved from the pension phase to the accumulation phase from 9 November 2016 until 30 June 2017.

  This will ensure when assets are sold, only tax is paid on capital gains accruing after 1 July 2017.

Strategy/Action

All assets will need to be valued at 30 June 2017. This will be readily available for cash and shares. Property will require valuations by a qualified property valuer. Due to the high demand for this service please contact a valuer as soon as possible so that appropriate arrangements can be made. For example a valuation can be performed now and updated at 30 June 2017, for little extra work.

Once the market values are known a decision to elect the CGT relief will involve complicated calculations on an asset by asset basis. An election will need to be made by the time the 2017 superfund return is lodged.

In most instances it will make sense for CGT relief to apply for those assets with unrealised capital gains at 30 June 2017.

For those assets with unrealised losses an election will probably not be beneficial.

We will assist you in making these CGT relief elections. In some circumstances it is going to be difficult to make a decision because super members will be *required to look ahead at what their fund might look like in 2 or 3 years time when they might want to sell the investment they have sought CGT relief on.*

- SMSF's will no longer be permitted to use the segregated method where a member has a more than $1.6 million super balance (across multiple funds) and the member is in pension phase.

  Strategy/Action

  For those with super balances in excess of $1.6 million and who wish to quarantine or segregate their pension assets from their accumulation assets (as there is no limit on the growth of the pension account once it has commenced and the earnings of the pension assets will be tax free) a second SMSF will be required, as mentioned earlier.

  Another option is that both pension and accumulation can be held in the one fund, but the assets will be pooled, and the earnings and tax are based on a proportionate method.

1 JULY 2018

- Individuals with a super balance of less than $500,000 will be allowed to make catch-up concessional contributions to their superannuation. Unused concessional contribution cap amounts can be carried forward for up to five years.

  Strategy/Action

  This could be beneficial where an individual had made a large capital gain and wishes to minimise their tax liability by making up to $125,000 of concessional contributions in the same year as the gain has been made.

DEFINITIONS (The following may help you understand some of the terminology used).

Superannuation includes funds either in what is known as pension or accumulation phase.

Pension phase occurs when a member elects to commence either an Account Based Pension (ABP) or Transitional Retirement Income Stream (TRIS):

ABP - Member must have satisfied one of three conditions of release:

- Reached preservation age (between ages 55 to 60, depending on when born) and intend not to work more than 10 hours per week.
- Reached age 60 and ceased an employment arrangement, or
- attained age 65.

TRIS - Member must have reached preservation age only.

Accumulation phase is typically where a member has not met a condition of release or reached preservation age and cannot commence a pension or withdraw a lump sum.

Also it may occur under the new rules where a member has a super balance of greater than $1.6 million and chooses to retain their funds in super rather than withdraw. Under the accumulation phase there is no compulsory requirement to withdraw from super until the member passes away.