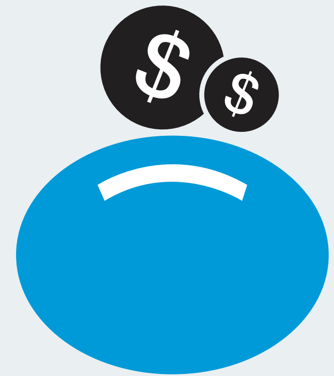
Stocktake on recent superannuation changes

by Daniel Butler, CTA, DBA Lawyers



The rules should encourage long-term savings rather than being a mechanism for governments to extract further tax revenue to balance their annual expenditure needs.

We have recently experienced substantial superannuation changes during the period of 1 July 2017 to 30 June 2018. Therefore, a brief "stocktake" of the changes introduced by the current Coalition Government is provided. A number of these policies were adverse to many members.

Prime Minister Malcolm Turnbull has said that the next federal election is to be held in 2019. As Labor may be elected, a brief "stocktake" of the key Labor Government proposals that will impact superannuation is also provided.

Despite the superannuation system being a long-term savings system, the Coalition Government has introduced ongoing unpredictability and costly changes.

Indeed, many members' superannuation savings are stuck in the system ("preserved") for the long-term — typically, until a member attains 60 years and retires. Members make their contributions and retain their investments in the superannuation system on the basis that the rules which applied when they put their money in will be the rules which apply when the time comes to take their money out. Any proposed adverse changes should therefore be accompanied by appropriate "grandfathering" provisions.

Members are at the mercy of government policy. Proposals that may not have even been notified to the electorate, such as the numerous adverse measures introduced by the Coalition Government's surprise announcement in the May 2016 federal Budget, followed repeated promises by the current Coalition Government that there would be no adverse change without prior consultation.

Not surprisingly, many members have lost confidence in the superannuation system due to the growing uncertainty and significantly reduced tax concessions that previously applied. Superannuation requires certainty and rules which remain stable. The rules should encourage long-term savings rather than being a mechanism for governments to extract further tax revenue to balance their annual expenditure needs.

Coalition Government recent adverse changes

Before discussing the current government's adverse changes, I would like to highlight one of the biggest mistakes relating to a proposed change that I have ever witnessed.

In its 3 May 2016 federal Budget, the Coalition Government introduced, by press release, a lifetime non-concessional contributions (NCC) cap of $500,000. That lifetime cap was designed to take into account all NCCs made on or after 1 July 2007. However, contributions made before the Budget announcement were "grandfathered" and would not have resulted in any excess NCCs.

That announcement was to have retrospective application for a period of almost nine years (ie 1 July 2007 to 3 May 2016 is around 3,230 days or just over 8.8 years). Thus, many people who had previously relied on the law during that period to make superannuation contributions were not to be permitted to make any further NCCs, since they would have exceeded their $500,000 lifetime cap. Despite that practical retrospective impact, the Coalition Government insisted that the proposed change was not retrospective. The Coalition Government took the view that the $500,000 lifetime cap was prospective only, as it only affected NCCs made after the 3 May 2016 Budget announcement. While the government argued that position, many disagreed. It followed repeated promises by the Coalition Government that the superannuation rules would not be changed adversely without prior consultation.

The controversial lifetime cap demonstrated how not to introduce superannuation reform. Indeed, this change attracted adverse feedback from many sectors of the superannuation industry, including the Coalition Government's own backbenchers. The Coalition Government eventually realised that the proposed $500,000 lifetime NCC limit was too contentious. On 15 September 2016, the Coalition Government dumped this change and replaced it with a $1.6m total superannuation balance limit that precluded further NCCs from 1 July 2017 where a member exceeded a $1.6m superannuation balance. Clearly, the $500,000 lifetime NCC limit policy process was flawed for, among other things:

- it was effectively retrospective for almost nine years for many people who had relied on the law in making contributions during that period;
- it was contrary to prior promises by the Coalition Government that there would be no adverse change without prior consultation; and
- it was not sound policy given that it had to be dumped after a four-month period after adverse feedback.

The Coalition Government's reputation suffered considerably from this poor policy decision which was badly implemented and which engendered significant distrust and uncertainty.

Changes introduced from 1 July 2017

The following is a brief "stocktake" of the main changes introduced by the Coalition Government from 1 July 2017.

$1.6m total superannuation balance

As discussed above, once a member's total superannuation balance hits $1.6m, there is no further opportunity to make any further NCCs. However, subject to certain regulations, if the member's balance subsequently falls below $1.6m, the member may again be permitted to contribute more NCCs.

$1.6m transfer balance cap

The $1.6m transfer balance cap (TBC) was introduced to limit the total amount that a member can transfer into the tax-free pension phase; now referred to as the retirement phase.

Previously, the earnings on assets supporting pensions, including transition to retirement income streams (TRISs), were tax-free without any maximum limit. The TBC measure caps the exempt current pension income (ECPI) exemption of each member to $1.6m of capital that can be used to commence a pension. Consequently, many members with pension balances above $1.6m prior to 1 July 2017 reduced their pension account to $1.6m by 30 June 2017.

Division 293 threshold

From 1 July 2017, the threshold at which high income earners pay an extra 15% additional contributions tax was reduced from $300,000 to $250,000.

Annual concessional contributions cap reduced to $25,000

From 1 July 2017, the annual concessional contributions (CC) cap was reduced to $25,000 each financial year (indexed in line with average weekly ordinary time earnings). Previously, the general limit for the prior financial year was $30,000 (or $35,000 for those aged 49 or above on 1 July 2016).

Tax deduction for personal superannuation contributions

From 1 July 2017, members have been eligible to claim an income tax deduction for personal superannuation contributions up to their CC cap without, broadly, having to satisfy the test that no more than 10% of earnings is from employee-like activities.

Transition to retirement income streams

As noted above, from 1 July 2017, the tax exemption on earnings derived from assets supporting a TRIS was removed. Therefore, earnings on TRIS assets are subject to tax (at the same rates as if these assets are in the accumulation phase) until the member satisfies a relevant condition of release.

However, on 22 June 2017, the Coalition Government introduced a new form of TRIS that can be in retirement phase and obtain a pension exemption. This is where the member has attained preservation age and retired (and notified the trustee) or attained 65. This is referred to as a "TRIS in retirement phase".

Broadly, a TRIS in retirement phase is treated in the same manner as an account-based pension that is subject to the ECPI exemption. Such a TRIS is also subject to the $1.6m TBC limit.

Labor Government's proposed superannuation changes

The following are some interesting extracts from the Labor Government's "Making superannuation fairer" fact sheet[1] to provide a background to Labor's superannuation policies:

> "Bill Shorten and Labor have led the policy debate on keeping our superannuation settings fit for purpose as our community ages and Australia's Budget faces new challenges.
>
> The contrast with the Turnbull Government's chaotic approach to superannuation couldn't be clearer.
>
> After relentlessly attacking Labor's proposed superannuation reforms, the Turnbull Government did an untidy about-face with a rushed and flawed package of super changes in the 2016 Budget.
>
> Malcolm Turnbull's retrospective changes were widely criticised for undermining confidence in the superannuation system, and were torn to shreds by his own backbench.
>
> Following months of wrangling and in-fighting, the Government then proposed a revised package that saw them dump and delay measures they had been defending as essential only weeks before. Australians looked on in amazement as Malcolm Turnbull and Scott Morrison proudly announced they had finally secured agreement for a revised plan – from George Christensen and their own backbench MPs.
>
> Labor's changes are responsible and fair. They are consistent with the superannuation reform principles we have been pursuing for more than a year: targeting concessions to where they are needed most while improving the Budget bottom line.
>
> Labor has consistently argued for reforms to tighten up superannuation tax breaks going to the top end. We have also made clear that our priority is helping low and middle income earners – particularly women – save enough for a comfortable retirement. The money that Government spends on superannuation tax concessions is money that cannot be spent elsewhere in our community, so this needs to be well targeted. We should be careful that at the same time as closing down one set of loopholes, we do not open up others."

If elected as a result of the 2019 federal election, at this stage, the Labor Party proposes to introduce the following changes that are largely expected to commence from 1 July 2019.

Franking credit refunds

From 1 July 2019, franking credit refunds to stop for self-managed superannuation funds (SMSFs). That is, subject to the Labor Government's pensioner guarantee commitment, where pensioners in receipt of Centrelink benefits prior to 28 March 2018 will have their franking credits grandfathered and will be eligible to receive such refunds in their SMSFs as well as personally.

Lowering the NCC cap to $75,000 per financial year

The current $100,000 per financial year NCC cap subject to the $1.6m total superannuation balance is to be reduced to $75,000.

Division 293 threshold

From 1 July 2019, the Labor Party proposes to reduce the Div 293 threshold from $250,000 to $200,000.

Other Labor proposals

Labor opposes the introduction of:

- catch-up concessional contributions over a five-year period that commenced on 1 July 2018 as introduced by the Coalition Government; and
- changes to tax deductibility for personal superannuation contributions as discussed above.

From 1 July 2019, it would also appear that a Labor Government will, if elected:

- increase the minimum superannuation guarantee contribution rate from its current 9.5% to 12% sooner than current legislative timetable where the

12% rate does not currently commence until 1 July 2025;

- further limit or stop limited recourse borrowing arrangements in SMSFs;
- limit negative gearing for residential rental properties; and
- tax non-fixed trust distributions at a minimum of 30% unless the distribution is from a fixed trust. It should be noted that many superannuation funds invest in unit trusts that do not qualify as fixed trusts. While the ATO currently has a more flexible approach in relation to superannuation funds that invest in unit trusts that are not fixed trusts, this administrative practice could be readily changed or be withdrawn by the ATO.

In contrast to the Coalition Government's surprise changes announced in May 2016, the Labor Government has provided prior notice in relation to its proposed changes outlined above. Naturally, if Labor is elected, advisers and members need to be aware that the next wave of superannuation adverse changes may not be that far away.

Conclusion

Australian politicians should not use superannuation as a short-term play. They must respect the long-term integrity of our financial system that plays a vital role in Australia's financial success and stability. Ongoing and unpredictable changes to the superannuation rules have a long-term adverse impact and many will adjust their retirement income plans accordingly. Greater stability and certainty is required to ensure that trust in the system can be restored and politicians should make long-term commitments to ensure Australia continues to benefit from a viable long-term and successful superannuation system.

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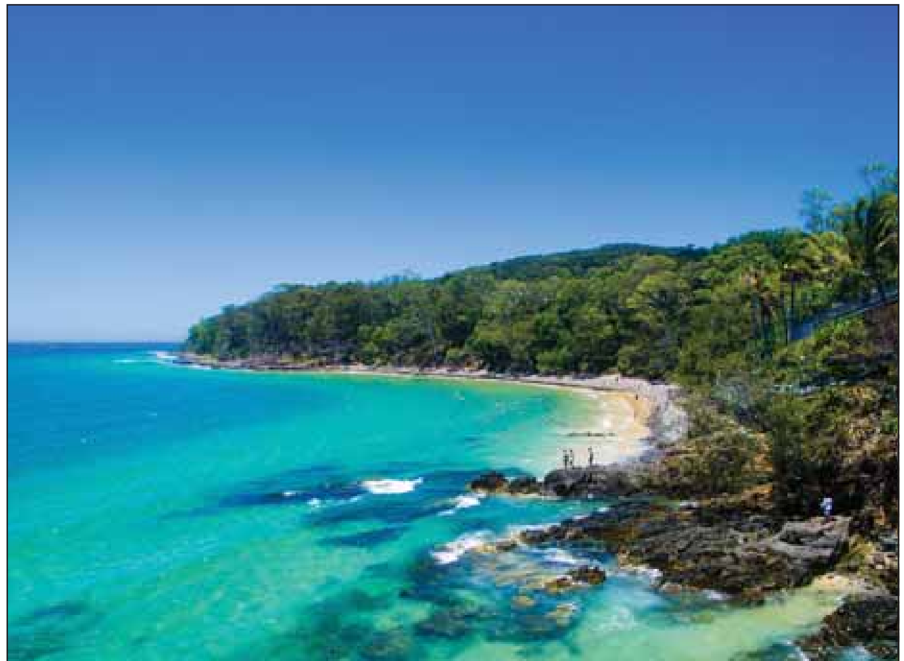
Reference

1 Available at www.alp.org.au/making_superannuation_fairer_fact_sheet (undated).



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