Federal Budget 2016

We're election bound!

A brief assessment of the Federal Government's third Budget since taking office in 2013, and the first under the new leadership of PM Turnbull and Treasurer Morrison. We look at the key issues impacting on your financial and future planning.

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A fairly friendly budget?

This was not your typical Budget. Already described as the 'super budget' given a lot of the measures that were introduced impacted superannuation.

Instead, the Treasurer Scott Morrison, attempted to build an election platform for the Government and overall, this Budget is quite fair to most people. While there were certainly some major alterations to superannuation, in other areas, such as Centrelink, there were only minor changes.

No changes to GST and negative gearing was left alone (although this is likely to remain an election issue with the Opposition wishing to reduce the concessions currently in place, particularly the 50% reduction in capital gains tax payable upon an assets disposal). These were fairly political hot potatoes and the government was not willing to touch these. Increase in funding for schools and hospitals (although not as much as the Opposition proposals), and beefed up spending for the ATO and ASIC as the tax and corporate regulators received a boost.

We've summarised some of the key points from the Budget below, but remember these are proposals only and are subject to the passing of legislation, which will remain challenging in the split Senate (double dissolution election on July 2?) and should be discussed with us.

In this summary document we focus on the key financial planning aspects of the Budget and how this may impact on you, our clients. We also consider other important changes to many broader funding programs that have been announced.

Below we list the key points as a summary, and follow this with a more in-depth explanation of some of those measures. It is not an extensive summary covering every point, however those we feel most relevant. If there are any points that are of interest to you either covered below or not, this is what we can discuss.

Please do not hesitate to contact us for further advice or analysis of what the budget means for you and your family.

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Key Financial Planning Points Summary

The Key Changes – Superannuation.

Concessional Contributions

- The limit of how much you can contribute will reduce to $25,000 from 1 July 2017. Currently this is $30,000 p.a. if under age 50 and $35,000 p.a. if over.
- You can contribute to super to age 75 (was 69).
- From 1 July 2017 if you have less than $500,000 in super and have not made the maximum contributions in previous years, you can make 'catch up' contributions limited in total to 5 prior years. This will assist people with the means that have had career breaks, large expenses that have limited their ability to cotribute to super, to top up their super in future years where there earnings allow.
    - E.g. Robert over the past 5 years contributed the following from his employer into super: $7,000 + $8,000 + $8,500 + $15,000 + $15,000 = $53,500. Over that time the maximum he 'could' have contributed was $125,000. Now the kids have finished private school, he has extra cash flow and can 'top up' another $71,500 if his budget allows it pre-tax via salary sacrifice over the coming years.
    - E.g. Sarah has spent 4 years as a mother to their 2 children. She has not made any super contributions. Over that time she 'could' have made upto a maximum of $100,000 of contributions. Sarah can if their buget allows it now she has returned to full time work make 'catch up' contributions up to this amount to assist in growing her super balance.
- Tax will be 15% on the contribution unless you earn more than $250,000. If you earn more than $250,000 the tax will be 30% on the contribution (previously $300,000). The threshold includes your total income plus super contributions.
    - E.g. Sue earns $200,000 from employment, $28,000 from an investment and made $25,000 super contribution pre tax (including her employer and salary sacrifice components). Her total assessable income is therefore $253,000 and will pay an additional 15% tax (30% in total) on her super contributions of $22,000.

Non Concessional Contributions

- From 7.30 pm on 3rd May 2016 a life time non concessional contribution limit will apply. **This cap is $500,000**.
- **The cap will take into account all contributions made since 1 July 2007.**
- The cap will be indexed in $50,000 increments in line with average weekly ordinary time earnings (AWOTE).

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- If you have exceeded the cap of $500,000 since 1 July 2007 you are **not** required to withdraw the excess. You however will not be able to make any future post-tax contributions.

Contributions (other)

- Threshold for a spouse contribution has increased. Previously, a partner may make a contribution to their spouses super account and receive a rebate for doing so (max $540). Spousal income needed to be under $13,800 p.a. to receive a rebate. This is now $37,000.

Transition to Retirement Pensions

- From 1 July 2017 the tax on earnings generated within the fund will move from Nil to 15% (i.e. same as accumulation phase).
- A transition to retirement pension is a pension drawn between age 56 and 65.
- The income drawn as a pension after age 60 will remain tax free.
- Converting accumulated super into pension phase and drawing a pension below age 60 will require a review to test the validity of continuing the strategy.

Pension Accounts capped at $1.6m

- From 1 July 2017, a $1.6m cap on the total amount of superannuation that can be used to commence a pension will be introduced. The tax on earnings generated within the fund will be Nil (funds under the $1.6m)
- The funds in excess of the cap will remain in accumulation and earnings will be taxed at 15%.
- For those entering retirement after 1 July 2017, any superannuation in excess of the cap can remain in accumulation, where earnings are taxed at 15%.
- For those with existing pensions on 1 July 2017, amounts in excess of the cap on this date will need to be rolled back into accumulation account.

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Key Points in Detail

Superannuation

Concessional (pre-tax) contribution cap reduced to $25,000

Effective 1 July 2017

The concessional contributions cap will reduce to $25,000 per annum for everyone regardless of age from 1 July 2017. Currently the concessional contributions cap is $30,000 for clients under age 50 and $35,000 for ages 50 and over.

From 1 July 2017, the Government will include notional (estimated) and actual employer contributions in the concessional contributions cap for members of unfunded defined benefit schemes and constitutionally protected funds.

For individuals who were members of a funded defined benefit scheme as at 12 May 2009, the existing grandfathering arrangements will continue.

Aspect Wealth Advisers Comment

The reduced concessional contributions cap of $25,000 does not apply until 2017-18. Clients should consider taking advantage of the current higher concessional cap of $30,000 (under age 50) and $35,000 (age 50 and over) in the 2015-16 and 2016-17 financial years.

Clients should review salary sacrifice arrangements and personal deductible super contributions to ensure they comply with the reduced concessional cap from 1 July 2017. May need to drip-feed contributions over a longer period in order to meet retirement goals as a result of the reduced concessional cap.

Catch-up concessional contributions

Effective 1 July 2017

Unused concessional contribution cap amounts will be able to be carried forward on a rolling basis over 5 consecutive years. This applies to unused cap amounts from 1 July 2017.

Access to unused cap amounts will be limited to individuals with a superannuation balance less than $500,000.

The Government states this measure will allow those who take breaks from the workforce the opportunity to 'catch-up' if they have the capacity and choose to do so.

The measure will also apply to members of defined benefit schemes.

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Aspect Wealth Advisers Comment

The ability to carry forward unused concessional cap amounts appears to apply to everyone who has contributed less than the concessional cap, not just those who take breaks from the workforce such as women and carers.

However, the reduction in the concessional cap to $25,000 pa will reduce the amount of concessional cap available to be carried forward.

Finally, it is unclear how the $500,000 threshold will be calculated and whether it will include previous withdrawals.

Lifetime cap for non-concessional (post-tax) contributions

Effective 7.30pm (AEST) 3 May 2016

A lifetime non-concessional contributions cap of $500,000 will be introduced effective Budget night, on 3 May 2016.

The $500,000 lifetime cap will take into account all non-concessional (post tax monies paid into super) contributions made on or after 1 July 2007. Contributions made before commencement (i.e. 7.30 pm AEST on 3 May 2016) cannot result in an excess of the lifetime cap, however those who have exceeded the cap prior to commencement will be taken to have used up their lifetime cap.

Non-concessional contributions made after Budget night that exceed the cap (taking into account all non-concessional contributions since 1 July 2007) will need to be removed or be subject to the current penalty tax arrangements.

The lifetime non-concessional cap will replace the existing annual non-concessional contributions cap of up to $180,000 per year (or $540,000 every 3-years under the bring-forward rule for individuals aged under 65). Those aged 65 to 74 who are currently limited to $180,000 per year will have access to the $500,000 cap without having to meet a work test.

Aspect Wealth Advisers Comment

To determine how much of the lifetime non-concessional cap has been utilised with prior non-concessional contributions, clients will need to add their non-concessional contributions since 1 July 2007 from all funds to determine how much counts towards their lifetime non-concessional cap (we can assist with this).

This may include components of a previously transferred UK pension fund.

Clients who have previously utilised the bring-forward provisions will need to carefully review their situation to determine whether they have exhausted their lifetime cap.

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Remove contribution eligibility requirements for those aged 65 to 74

Effective 1 July 2017

The current work test that applies for people making voluntary contributions between age 65 and 74 will be removed. This change will allow individuals to make contributions for a spouse aged under 75 without requiring the spouse to satisfy a work test.

The Government says this will simplify the superannuation system for older Australians and allow them to increase their retirement savings, especially from sources that may not have been available to them before retirement, including downsizing their home.

Aspect Wealth Advisers Comment

Clients are currently required to work 40 hours within 30 consecutive days in the financial year they make a contribution over the age of 65. This proposal will remove this requirement and make it easier for older clients to contribute to super.

When combined with the life-time non-concessional cap this proposal could allow non-working clients aged between 65 and 74 who were previously ineligible to contribute to make non-concessional contributions of up to $500,000 after 1 July 2017.

Introduce a $1.6 million superannuation transfer balance cap

Effective 1 July 2017

A cap will be introduced to restrict the total amount of superannuation that can be transferred from accumulation to pension phase to $1.6 million. Where an individual accumulates amounts in excess of $1.6 million, they will be able to maintain this excess in accumulation phase (where earnings will be taxed at the concessional rate of 15 per cent).

The cap will be indexed in $100,000 increments in line with the consumer price index.

Existing pension balances

Members already in pension phase as at 1 July 2017 with balances in excess of $1.6 million will need to either:

• transfer the excess back into an accumulation; or

• withdraw the excess amount from their superannuation.

Individuals who breach the cap will be subject to a tax on both the amount in excess of the cap and the earnings on the excess amount similar to the tax treatment that applies to excess non-concessional contributions.

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The Government has also confirmed 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 (see Defined Benefit Scheme Changes below).

Aspect Wealth Advisers Comment

This proposal will allow couples to have a combined pension balance of up to $3.2 million. How many people will this really impact? Not many. However, where most of a couple's superannuation savings are in one spouses name the $500,000 lifetime non-concessional cap will restrict a couple's ability to equalise their benefits to take full advantage of the transfer balance cap.

The requirement for members with balances already in excess of $1.6 million to either withdraw or transfer the amount in excess of the cap back to superannuation means that people with pension account balances in excess of $1.6 million have not been grandfathered from these changes.

Additional 15% contributions tax: threshold reduces to $250,000

Effective 1 July 2017

Division 293 tax, which is an additional 15% contributions tax payable by high income earners with income exceeding $300,000, will apply to those with income exceeding $250,000 from 1 July 2017.

The Government claims reducing the Division 293 tax income threshold will improve sustainability and fairness in the superannuation system by limiting the effective tax concessions provided to high income individuals.

It is important to note the definition of income for Division 293 purposes includes:

• Taxable income (including the net amount on which family trust distribution tax has been paid)

• Reportable fringe benefits

• Total net investment loss (including net financial investment loss and net rental property loss)

• Low tax contributions (non-excessive concessional contributions) including super guarantee, salary sacrifice and personal concessional contributions.

Division 293 tax will apply to any low tax contributions that exceed the $250,000 threshold, assuming they form the top slice of income.

Transition to retirement pensions: removal of earnings tax exemption

Effective 1 July 2017

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The tax exempt status of income from assets supporting transition to retirement (TTR) income streams will be removed from 1 July 2017. Earnings will then be taxed at 15 per cent. This change applies irrespective of when the TTR income stream commenced, i.e. no grandfathering applies.

The Government states that reducing the tax concessional nature of transition to retirement income streams will ensure they are fit for purpose and not primarily accessed for tax minimisation purposes.

Aspect Wealth Advisers Comment

Taxing earnings on TTR income streams significantly reduces the tax effectiveness of strategies such as TTR and salary sacrifice. For clients aged 60 or over, TTR strategies may still be worthwhile as pension payments are tax free and allow tax effective salary sacrifice contributions. However, for clients under age 60, the tax benefits are minimal.

The taxation of earnings in pension phase will only apply to 'transition to retirement' income streams where the client has reached preservation age but not yet retired. Presumably income streams where the client has met a full condition of release such as retirement will continue to have the earnings tax exemption apply. Clients may look at arrangements involving ceasing a gainful employment arrangement over age 60 or ceasing work and declaring permanent retirement to meet the retirement condition of release.

Increased access to spouse superannuation tax offset

Effective 1 July 2017

The current spouse superannuation tax offset will be available to more people due to an increase in the spouse income threshold from 1 July 2017.

The income threshold for the spouse superannuation tax offset is increasing from $10,800 to $37,000.

A contributing spouse will be eligible for an 18 per cent offset worth up to $540 for contributions made to an eligible spouse's superannuation account.

Aspect Wealth Advisers Comment

Currently the spouse superannuation tax offset reduces where the spouse's income exceeds $10,800 and cuts out altogether when their income reaches $13,800.

If the same methodology applies, the tax offset would reduce where the spouse's income exceeds $37,000 and cut out altogether at $40,000.

The ATO will determine a person's eligibility for the LISTO and advise their superannuation fund annually. The fund will contribute the LISTO to the member's account.

Low income superannuation tax offset

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Effective 1 July 2017

A Low Income Superannuation Tax Offset (LISTO) will be introduced from 1 July 2017 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 up to a cap of $500. The LISTO will apply to members with adjusted taxable income up to $37,000 that have had a concessional contribution made on their behalf.

Aspect Wealth Advisers Comment

A good measure extending the current arrangement to ensure individuals are not paying a higher tax rate on their super contributions than they are personally.

Extend deductions for personal contributions

Effective 1 July 2017

Australians under 75 will be able to claim an income tax deduction for any personal superannuation contributions made to a complying superannuation fund up to their concessional cap. This effectively allows all individuals, regardless of their employment circumstances, to claim a deduction for their personal contributions up to the value of the concessional cap.

To access the tax deduction, individuals will need to lodge a notice of their intention to claim the deduction with their superannuation fund or retirement savings provider prior to lodging their tax return. These amounts will count towards the individual's concessional contributions cap, and be subject to 15 per cent contributions tax. Individuals can choose how much of their contributions to deduct however if they end up exceeding their concessional cap the deduction claimed on the excess contributions will have no effect as these amounts will be included back into the member's assessable income.

Aspect Wealth Advisers Comment

This announcement will dramatically simplify the eligibility requirements for a member to qualify to claim a deduction for a personal super contribution. The requirement to not be an employee during the financial year or to satisfy the 10% test will be replaced with a simple requirement to be under age 75.

The announcement also gives employees more flexibility and allows them to make personal deductible contributions in addition to super guarantee and salary sacrifice contributions, to use up any unused concessional cap at the end of the year.

Defined benefit scheme changes

Effective 1 July 2017

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The Government has announced a range of reforms to the taxation of benefits paid from defined benefit schemes and constitutionally protected funds to ensure equitable treatment of members in these funds and accumulation.

$1.6 million transfer balance cap

To broadly replicate the effect of the proposed $1.6 million transfer balance cap, the Government has announced that pension payments over $100,000 per annum paid to members of unfunded defined benefit schemes and constitutionally protected funds providing defined benefit pensions, will continue to be taxed at full marginal rates, however the 10 per cent tax offset will be capped at $10,000 from 1 July 2017.

For members of funded defined benefit schemes, 50 per cent of pension amounts over $100,000 per annum will now be taxed at the individual's marginal tax rate.

Taxation

Reducing the company tax rate to 25 per cent

Effective from 1 July 2016

The company tax rate will be reduced to 25 per cent over 10 years. Currently, small business companies with aggregated turnover less than $2 million pay tax at rate of 28.5%. Franking credits will be able to be distributed in line with the rate of tax paid by the company making the distribution.

PROPOSED REDUCTION TO COMPANY TAX RATES

Financial year	Companies with annual aggregated turnover of less than	Applicable company tax rate
2016-17	$10 million	27.5%
2017-18	$25 million	27.5%
2018-19	$50 million	27.5%
2019-20	$100 million	27.5%
2020-21	$250 million	27.5%
2021-22	$500 million	27.5%
2022-23	$1 billion	27.5%
2024-25	All companies	27%
2025-26	All companies	26%
2026-27	All companies	25%

Aspect Wealth Advisers Comment

We are largely in favour of this measure. Whilst socially it appears as 'letting the rich get richer', it is aimed at moving Australia's corporate tax rate to more in line with OECD average. Remembering that the top 50 companies in Australia all have turnover of more than $1bn therefore this is not really benefiting the 'big end of town'.

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Personal income tax reduction

Effective 1 July 2017

The Government will increase the 32.5 per cent personal income tax threshold from $80,000 to $87,000 from 1 July 2016.

This measure will reduce the marginal rate of tax on income between $80,000 and $87,000 from 37 per cent to 32.5 per cent. This will ensure that the average full-time wage earner will not move into the second highest tax bracket in the next three years.

A taxpayer earning $87,000 will save $315 per annum as a result of the change to the personal income tax threshold.

PERSONAL TAX RATES

Current tax rates 2015-16		Proposed tax rates 2016-17	
Taxable Income	Tax Payable *	Taxable Income	Tax Payable *
$0 - $18,200	0%	$0 - $18,200	0%
$18,201 - $37,000	19% over $18,200	$18,201 - $37,000	19% over $18,200
$37,001 - $80,000	$3,572 + 32.5% over $37,000	$37,001 - $87,000	$3,572 + 32.5% over $37,000
$80,000 - $180,000	$17,547 + 37% over $80,000	$87,000 - $180,000	$19,822 + 37% over $87,000
$180,000+	$54,547 + 45% over $180,000	$180,000+	$54,232 + 45% over $180,000

The temporary budget repair levy will also drop off as planned at the end of this tax year. It is not a tax cut for those on the highest tax bracket, it was always slated as ‘temporary’ and the treasurer has confirmed its removal.

Social Security

Simplifying student payments

Effective 1 January 2017

Means testing arrangements for students and other payment recipients will be simplified from 1 January 2017. The changes include aligning the:

• assets test for all Youth Allowance and Austudy recipients, including those partnered to a Social Security or Veterans’ Affairs income support recipient

• means test rules used to assess interests in trusts and private companies for all student payment recipients, including independent Youth Allowance and ABSTUDY recipients

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• social security benefits and ABSTUDY income test treatment of gift payments from immediate family members with existing pension rules, and

• Family Tax Benefit (FTB) income test and youth Parental Income Test, and authorising the use of FTB income details for the youth Parental Income Test

Effective 1 January 2019

• Student income support recipients will be automatically issued with a Health Care Card from 1 January 2019. This change will allow Youth Allowance (student), Austudy and ABSTUDY recipients to be automatically issued a Health Care Card at the same time as their grant of payment.

Social security savings

A range of social security measures aimed at savings to fund the National Disability Insurance Scheme are proposed.

• New welfare recipients from 20 September 2016 will not be eligible for carbon tax compensation.

• Backdating provisions for new Carer Allowance claims will be aligned with other social security payments. From 1 January 2017, Carer Allowance will be payable to eligible applicants from the date of the claim, or the date they first contact the Department of Human Services.

• Increased reviews of Disability Support Pension recipients by assessing their capacity to work.

If you have any questions relating to the above information, or would like a more detailed assessment of how the Budget outcomes may impact on your particular circumstances, please do not hesitate to contact us. Additionally, if there is an area of the Budget not addressed above you may have questions on, we would be more than happy to discuss.

Sources:

- Treasury Budget Papers 2016
- FirstTech: 2016 Federal Budget Briefing
- IOOF Budget Update
- BT Budget Summary