



Federal Budget 2006

Delivering a simpler taxation system for superannuation

The Federal Budget announcements were significant for members of superannuation funds. Although these changes are proposals at this stage, if passed as law, they are significant changes to the Australian superannuation industry.

An overview of the changes to taxation on superannuation

The proposed changes to superannuation taxes will result in a simpler system whereby most retirees will pay less tax. Some complexity will remain though, especially for those drawing benefits before age 60.

Currently, in Australia, superannuation is taxed at three levels: on contributions, on investment earnings, and on benefit withdrawal. While taxation at the contribution and earnings stages will remain, the Government has proposed to end taxation at the benefit withdrawal stage for most benefits.

From 1 July 2007, it is proposed that:

- Superannuation benefits paid from a complying fund will be tax free for people aged 60 or over. The benefit will be tax free whether it is taken as a lump sum or pension.
- Reasonable Benefits Limits (RBLs) will be abolished i.e. "excessive" benefit taxes will be removed.
- Benefits paid to people under age 60 will be taxed under streamlined arrangements.
- Pre-tax contribution limits will change from the current age-based limits approach. Pre-tax contributions include Salary Sacrifice contributions, 9% SG company contributions and company contributions made for defined benefits. All pre-tax (salary sacrifice) contributions up to \$50,000 will be taxed at 15% and pre-tax contributions in excess of \$50,000 will be taxed at the highest marginal income tax rate. Note that there will be some transitional relief to permit individuals currently aged 50 and over to contribute up to \$100,000 per year until 2011/12.

- The maximum amount of post-tax contributions that can be made will be \$150,000 per year, although some advance contributions are permitted (see next page).

Highlights

- A simpler taxation system for superannuation
- Most retirees will pay less tax when receiving their benefit
- Reasonable Benefit Limits will be abolished
- Pre-tax (salary sacrifice and company) contributions will be limited to \$50,000 per year
- Post-tax contributions will be limited to \$150,000 per year, although some advance contributions will be allowed
- From 1 July 2006, income tax thresholds become broader and tax rates on income above \$75,000 are reduced
- Easier to satisfy the assets test to receive the Commonwealth Government age pension

Other key proposals (yet to be legislated)

Greater flexibility in withdrawing benefits

From 1 July 2007, there will be no requirement to withdraw your superannuation benefit after age 65. Individuals will no longer have to satisfy a work test in order to keep their benefits in a superannuation fund after age 65.

Assets test allowing additional assets

From 20 September 2007, retirees will lose \$1.50 rather than \$3 in the Commonwealth Government's age pension for every \$1,000 of assets above the assets test free threshold. A single retiree home owner will be able to have an additional \$165,000 of assets before losing entitlement to the age pension. For couples, the additional amount is \$275,000.



Simplification of income streams

For new pensions commencing on or after 1 July 2007, there will be rules on minimum amounts payable each year but no maximum limits will apply. Importantly, earnings on assets supporting pensions will remain tax-exempt.

Employer Eligible Termination Payments (ETPs)

It will no longer be possible to rollover employer ETPs, such as redundancy payments above the tax-free amount, to a superannuation fund. However, these may be contributed as an after-tax lump sum amount to a super fund.

Implications

Advance post-tax contributions

There is some flexibility as to how the maximum post-tax contribution limit of \$150,000 per year is applied. In particular:

- For the 2005/2006 year, post-tax contributions made prior to the Budget night (9 May 2006) will not be counted;
- For the remainder of the 2005/2006 year, and in later years, up to \$150,000 of post-tax contributions may be made; and
- If the cap of \$150,000 is not used in any year, then the unused amount cannot be carried forward into a later year.

In some years, post-tax contributions in excess of \$150,000 may be made. These are treated as advance contributions, and the cap available for the following two years will be reduced. For example, a post-tax contribution of \$450,000 could be made in 2005/06, in which case the cap of \$150,000 for the three years (2005/06, 2006/07, 2007/08) would be fully used. No further post-tax contributions could then be made until 1 July 2008.

Timing of Retirement

The other changes will not come into force until 1 July 2007. Reductions in tax on benefits, and removal of RBLs, will not be available to benefits received prior to that date. For benefits paid to members aged less than 60, tax will still be payable although the method for calculating this tax will be simplified.

Contribution splitting

Due to the removal of tax on superannuation benefits for individuals aged 60 and over from 1 July 2007, contribution splitting (which was only introduced from 1 January 2006) will no longer be required to access two tax free thresholds or two Reasonable Benefit Limits for people taking benefits after age 60. However, contribution splitting may still be tax effective where a person or their spouse intends to take their superannuation benefit (in either lump sum or pension form) before age 60.

Changes to Personal Income Tax Rates

The Government announced changes to both the marginal tax rates and the thresholds, effective 1 July 2006. These changes, which will benefit most taxpayers, replace those announced in last year's Budget. The marginal tax rates at the upper end of the income scale have been reduced. In addition, the Government has increased the threshold amounts.

The proposed new income tax scale is as follows:

Current		From 1 July 2006	
Tax thresholds (\$)	Tax rate %	Tax thresholds (\$)	Tax rate %
0 - 6,000	0	0 - 6,000	0
6,001 - 21,600	15	6,001 - 25,000	15
21,601 - 63,000	30	25,001 - 75,000	30
63,001 - 95,000	42	75,001 - 150,000	40
95,001+	47	150,001+	45

Next steps

As the detail around these Budget announcements becomes clearer, the Trustee will be updating systems and communications to allow the new Budget initiatives to be implemented.

More details will be provided as the details become available.