Federal Budget 2017

May 2017

BT Financial Group

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The Treasurer, the Hon Scott Morrison, has handed down his second Federal Budget in Canberra overnight. He spoke of this Budget being about fairness, security and opportunity with the Government focussing on guaranteeing essential services, tackling the cost of living and ensuring the Government lives within its means.

Following extensive changes to superannuation in the 2016 Federal Budget, there were only a handful of new measures for superannuation this time around. As anticipated, two of the super measures linked in to the Government's housing affordability policy with the only sting being for SMSF members whose fund has limited recourse borrowing arrangements.

The following Budget update looks broadly at the measures announced that impact on SMSFs. It is important to understand that most of these measures will need to be passed by Parliament before they become law.

If you think that these changes may impact on your retirement or investment plan, it is important to speak with your adviser before acting.

Key points on Superannuation

Integrity of limited recourse borrowing arrangements

Effective Date: 1 July 2017

The member's total superannuation balance will include the outstanding balance of the LRBA

The Government intends to amend the existing transfer balance cap and total superannuation balance provisions to take into account limited recourse borrowing arrangements (LRBAs).

From 1 July 2017, for members of a SMSF or Small APRA Fund (SAF) with a limited recourse borrowing arrangement:

- the member's total superannuation balance will include the outstanding balance of the LRBA, and
- the repayment of the principal and interest of the LRBA from the member's accumulation account will be counted towards their transfer balance cap.

These changes are being made to prevent LRBAs being used to circumvent contribution caps by effectively transferring growth in assets from the accumulation phase to the retirement phase without having this growth assessed against an individual's transfer balance cap.

On 27 April 2017, the Government issued for consultation draft legislation to introduce these proposed changes. For further details read the Treasury announcement, draft legislation and explanatory memorandum.

What does this mean for SMSF trustees?

- Assets effectively transferred from the accumulation phase to the retirement phase of an SMSF or SAF to repay some or all of a LRBA will count towards the relevant SMSF or SAF members' transfer balance caps.
  - Where members have maintained an LRBA into retirement, it will be necessary to monitor the source of repayments and, where these come from the accumulation phase, it will be necessary to monitor the member's transfer balance cap and, if necessary, commute some of the member's income stream.
- The gross, not the net, value of an asset subject to a LRBA will be included in the relevant SMSF or SAF members' total superannuation balance. Including the outstanding balance of LRBAs in a member's total super balance, may result in the member's total super balance exceeding $1.6m on 30 June, meaning in the following financial year they may be unable to:
  - make personal after-tax (non-concessional) contributions to superannuation
  - take advantage of the carry forward of unused concessional contributions provisions
  - claim a tax offset for contributions made to their spouse's superannuation.
- The proposed changes generally make LRBAs less attractive.

Integrity of non-arm's length arrangements

Effective Date: 1 July 2018

The existing non-arm's length income provisions will be amended

From 1 July 2018, the Government intends to amend the existing non-arm's length income provisions to ensure that expenses that would normally apply in a commercial transaction are included when considering whether the transaction is being made on a commercial basis.

These changes are being made to reduce opportunities for individuals to use related party transactions on non-commercial terms to increase their superannuation savings.

What does this mean for SMSF trustees?

> When SMSF trustees are dealing with related parties, a more complex test will be involved to determine whether the transaction has been made at arm's length.

> The measure appears to tighten the current arm's length income rules.

— When SMSFs are dealing with related parties, greater care will need to be taken to ensure that the fund complies with the arm's length rules, to ensure income is not taxed at a penalty tax rate.

Improving external dispute resolution – new single complaints body

Effective Date: 1 July 2018

The Government intends to introduce a new framework for dispute resolution from 1 July 2018 with the establishment of the Australian Financial Complaints Authority (AFCA).

AFCA will be an industry funded one-stop shop for complaints resolution for all financial and superannuation disputes. AFCA will replace the Financial Ombudsman Service, the Credit and Investments Ombudsman and the Superannuation Complaints Tribunal (SCT). The SCT will no longer operate from 1 July 2020.

The AFCA is intended to provide financial services consumers, small businesses and retail investors with access to a free, fast and binding dispute resolution service. This new dispute resolution body will hear individual consumer/investor and small business disputes of higher values than are currently permitted under the three existing schemes. Individuals found to have wrongfully suffered losses will also have access to more appropriate levels of compensation.

All Australian Financial Services Licensees will be required to be members of AFCA, and its decisions will be binding on all financial services firms.

What does this mean for SMSF trustees?

> SMSF members will not have access to the new dispute resolution body, just as they do not currently have access to the SCT, however, SMSF trustees would have access to the new body in relation to services provided by an AFSL holder.

Productivity Commission review of competition in the financial system

Effective Date: 1 July 2017

Following on from the Productivity Commission (PC) review into the efficiency and competitiveness of Australia's super system, the Government has tasked the PC to complete a review on of the state of competition in the financial system.

The review will evaluate competition in the financial system with a view to improving consumer outcomes, the productivity and international competitiveness of the financial system and economy more broadly, and supporting ongoing financial system innovation, while balancing financial stability objectives.

The review is set to commence on 1 July 2017 and the PC will have 12 months to report outcomes to Government.

Key points on Taxation

The Medicare Levy will increase from 1 July 2019

Increase in Medicare Levy

Effective Date: 1 July 2019

From 1 July 2019, the Medicare Levy will increase to 2.5% (from 2%). This increase is to ensure that the National Disability Insurance Scheme is fully funded. Other tax rates that are linked to the top marginal tax rate, such as the fringe benefits tax rate, will also be increased.

The table below shows the additional Medicare Levy payable from 1 July 2019.

Income	$50,000	$75,000	$100,000	$150,000
Additional Medicare Levy	$250 pa	$375 pa	$500 pa	$750 pa

What does this mean for you?

> An increase in the Medicare Levy will impact those liable to pay the levy from 1 July 2019. On an income of $80,000 the increase in Medicare levy will be $400 per year.

Increase in the Medicare Levy low income thresholds

Effective Date: 1 July 2016

The Government has announced increases to the Medicare Levy low income thresholds that apply for the current financial year (ending 30 June 2017).

The Medicare Levy low income thresholds will be increased as follows:

- $21,655 for individuals (previously $21,335)
- $36,541 for couples with no children (previously $36,001)
- $34,244 for pensioners eligible for the Seniors and Pensioners Tax Offset (previously $33,738)
- $47,670 for senior and pensioner couples with no children (previously $46,966)

For families and senior and pensioner couples with children, the additional amount of threshold for each dependent child or student will be increased to $3,356 (up from $3,306)

What does this mean for you?

- If your income is below the relevant threshold you won't need to pay Medicare levy this financial year.

The CGT discount will be increased for individuals investing in affordable housing

Increase in CGT discount for investments in affordable housing

Effective Dates: 1 July 2017 and 1 July 2018

Resident individuals will be entitled to an increase in the CGT discount for investments in affordable housing from 1 July 2018. The CGT discount for eligible investments will increase from 50% to 60%.

To qualify for the higher discount, housing must be provided to low to moderate income tenants, with rent charged at a discount below the private rental market rate. The affordable housing must be managed through a registered community housing provider and the investment held for a minimum period of three years.

The Government will consult further on the implementation of this policy, including on the precise definition of affordable housing and tenant eligibility, and what qualifies as rent charged below the market rate.

The CGT discount will also be available through Managed Investment Trusts (MITs) from 1 July 2017. An MIT will be able to acquire, construct or redevelop the property but must derive at least 80% of its assessable income from affordable housing. Qualifying housing must be provided to low to moderate income tenants, with rent charged at a discount below the private rental market rate.

In order for investors to receive concessional taxation treatment through a MIT, the affordable housing must be available for rent for at least 10 years.

Resident investors in these MITs will continue to be taxed on investment returns at their marginal tax rates. Income from capital gains will be eligible for the increased CGT discount of 60% (rather than the standard 50%), where applicable. An increased CGT discount will not apply to super funds.

What does this mean for SMSF trustees?

> SMSFs will not benefit from the increase in the CGT discount, however, members investing in their own names may benefit from this change.

Disallowing the deduction of travel expenses for residential investment properties

Effective Date: 1 July 2017

Deductions for travel expenses related to inspecting, maintaining or collecting rent for a residential rental property will be disallowed from 1 July 2017.

What does this mean for you?

> 2016/17 will be the last year you will be eligible to claim a tax deduction for expenses related to inspecting, maintaining or collecting rent for a residential rental property.

Reducing the CGT concessions available to foreign investors

Effective Dates: 9 May 2017 and 1 July 2017

From 7.30pm on 9 May 2017, access to the CGT main residence exemption will be denied to foreign and temporary tax residents. The exemption will remain available until 30 June 2019 for existing properties held prior to this time.

From 1 July 2017, the following proposed changes will also impact foreign tax residents:

- the CGT withholding rate will increase from 10% to 12.5%, and
- the CGT withholding tax threshold will fall from $2m to $750,000.

What does this mean for SMSF trustees?

- This measure could have an impact on property prices through a reduction in demand from foreign investors.

Tightening the small business CGT concessions

Effective Date: 1 July 2017

The small business capital gains tax (CGT) concessions will be amended to ensure that the concessions can only be accessed in relation to assets used in a small business or ownership interests in a small business.

According to the budget papers some taxpayers are able to access these concessions for assets which are unrelated to their small business, for instance through arranging their affairs so that their ownership interests in larger businesses do not count towards the tests for determining eligibility for the concessions.

The existing small business CGT concessions will continue to be available to small business taxpayers with aggregated turnover of less than $2 million or business assets less than $6 million.

What does this mean for SMSF trustees?

- SMSF members planning to make use of the CGT small business concession to make contributions to their fund will need to be aware of the more stringent requirements.

Housing affordability

Individuals age 65 or over will be able to make a non-concessional contribution of up to $300,000

Contributing the proceeds of downsizing to superannuation

Effective Date: 1 July 2018

From 1 July 2018, individuals aged 65 or over will be allowed to make a non-concessional contribution into superannuation of up to $300,000 from the proceeds of selling their principal residence. Contributions made under the proposed downsizing provisions will be exempt from the existing contribution rules for individuals aged 65 and older. The existing age test, work test and $1.6 million total super balance restrictions that apply to ordinary non-concessional contributions will also not apply to contributions made under these provisions.

Contributions made as a result of downsizing will be in addition to any other voluntary contributions that individuals are able to make under the existing contribution rules and caps.

To be eligible for this new measure, individuals must have owned their principal residence for at least 10 years. Both members of a couple will be able to take advantage of this measure for the same home, meaning $600,000 per couple can be contributed to superannuation through the downsizing provisions.

While the restrictions on non-concessional contributions for individuals with super balances above $1.6 million will not apply to contributions made under this new downsizing cap, the general transfer balance cap for the purposes of commencing an income stream will still apply.

In addition, sale proceeds contributed to superannuation under this measure will count toward the assets test for Social Security purposes.

What does this mean for SMSF trustees?

> Members who are currently unable to contribute to superannuation because of the existing restrictions and caps may be able to make contributions to super, provided the proceeds are from the sale of their home and eligibility criteria are met.

> Members receiving Social Security payments, such as the Age Pension, may have their payments reduced as the contribution will generally increase the value counted under the means tests.

First Home Super Saver Scheme

Effective Date: 1 July 2017

From 1 July 2017, individuals will be able to make voluntary contributions to superannuation of up to $15,000 per year and $30,000 in total for the purposes of purchasing a first home. The contributions can be made using before-tax or after-tax money (i.e. concessional or non-concessional contributions) and must be made within an individual's existing contribution caps.

From 1 July 2018 onwards, individuals will be able to withdraw these contributions and their associated deemed earnings from superannuation to fund a first home deposit. The taxable component of any withdrawals will be taxed at an individual's marginal tax rate, less a 30% tax offset. No tax will be payable on the tax free component of any withdrawals.

The amount of earnings that can be released will be calculated using a deemed rate of return based on the 90 day Bank Bill rate plus 3%.

Withdrawals from superannuation for the purposes of purchasing a first home will not impact the individual's social security entitlements such as HECS/HELP repayments, family tax benefit or child care benefit.

The ATO will be responsible for administering the new First Home Super Saver Scheme and as such will assess eligibility for withdrawing amounts for the purposes of purchasing a first home as well as calculating the amount that can be released. Superannuation funds will need to respond to a release request authorised by the ATO (it is expected the ATO would leverage the existing release authority process).

First Home Super Saver scheme to be administered by ATO

The ATO will also be responsible for ensuring that individuals actually use the proceeds they have withdrawn from superannuation to purchase their first home.

The First Home Super Saver Scheme differs to the First Home Saver Account (FHSA) regime that was abolished in 2015. FHSA's were separate stand alone accounts managed by financial institutions which required individuals to contribute a minimum of $1,000 from after-tax income each financial year. Salary sacrifice contributions to FHSA were not possible, and accounts were required to be held for 4 years before being eligible to withdraw. The First Home Super Saver Scheme utilises the existing superannuation framework to derive tax incentives, including the use of salary sacrifice arrangements.

For an individual with a taxable income of $80,000 p.a. making annual salary sacrifice contributions of $10,000, the following example highlights the potential benefits of the First Home Super Saver Scheme compared to saving via a standard deposit account.

	2017/18	2018/19	2019/20	2020/21
Annual salary sacrifice	$10,000	$10,000	$10,000	$0
Amount available for deposit (after-tax)	$8,312	$16,983	$25,542	$26,276
Increase in savings from first home deposit*	$1,719	$3,711	$5,555	$6,029

* Compared to saving in a standard deposit account

Source: First Home Saver Super Scheme Estimator

What does this mean for SMSF trustees?

> The First Home Super Saver Scheme could boost the savings you can put towards a deposit for your first home by at least 30% compared with saving through a standard deposit account.

> If your employer offers salary sacrificing, you can take advantage of these arrangements to make additional concessional contributions towards funding your first home deposit

> If you are self-employed, or do not have access to salary sacrificing arrangements through your employer, you can make after-tax contributions to super and subsequently claim a tax deduction on these contributions, meaning savings are effectively derived from your before-tax income.

> You and your partner can both take advantage of this scheme to buy your first home together.

Key social security changes

Reinstating the Pensioner Concession Card

Effective Date: 1 July 2017

Pensioners who were no longer entitled to the Age Pension following changes to the pension assets test from 1 January 2017 will have their Pensioner Concession Card (PCC) reinstated.

What does this mean for you?

> If you are eligible to have your Pensioner Concession Card reinstated, you will be able to access health care and certain goods and services (e.g. electricity and gas bills, property and water rates and public transport fares) at a reduced cost.

Enhanced Residency Requirements for Pensioners

Effective Date: 1 July 2018

From 1 July 2018, claimants of Age Pension and Disability Support Pension (DSP) will be required to have 15 years of continuous Australian residence before being eligible to receive the pension unless they have either:

- 10 years continuous Australian residence, with five years of this residence being during their working life (16 years to Age Pension age); or
- 10 years continuous Australian residence, without having received an activity tested income support payment for a cumulative period of five years.
  - Currently, to be eligible to receive an Age Pension or DSP, you need to have been an Australian resident for at least 10 years in total with continuous residency of at least 5 years.
  - Existing exemptions for DSP applicants who acquire their disability in Australia will continue to apply.

What does this mean for you?

- If you have less than 15 years of continuous Australian residence you may not be able to access the Age Pension or Disability Support Pension (DSP) as early as you previously would have been able to.

Energy Assistance Payment

Effective Date: 2016-17

- A one off Energy Assistance Payment of $75 for singles and $125 per couple will be provided in 2016-17 for those eligible for qualifying payments on 20 June 2017.
- Qualifying payments include the Age Pension, Disability Support Pension, Parenting Payment Single, the Veterans' Service Pension and the Veterans' Income Support Supplement, Veterans' disability payments and War Widow(er)s Pension.

What does this mean for you?

If you are in receipt of a qualifying payment, you will be entitled to an additional payment from the Government to assist you to pay your energy bills.