# 2017

# FEDERAL BUDGET GUIDE

## BUDGET USES THE POWER OF SUPER TO GIVE HOUSING AFFORDABILITY A DOUBLE PUNCH

'Fairness', 'security' and 'opportunity' were the words Treasurer Scott Morrison used to characterise his second Budget. The benefit of more favourable global economic conditions means the budget doesn't need to bite as hard as recent Budgets have proposed and there is also a clear intention to spread the task of 'budget repair' across the community more generally.

In contrast to last year's budget, which saw the biggest shake-up to super in a decade, the 2017 Budget proposes using super as a tool to help tackle issues of housing affordability and supply. Two significant initiatives intertwine home ownership with the tax-advantaged power of super.

### SUPER SAVINGS BOOST FOR FIRST HOME BUYERS

The 'First Home Super Saver Scheme' uses the tax advantages of super to help first home buyers. If the Budget is passed by the Senate, from 1 July this year you'll be able to use your super to turbocharge your saving for a home deposit for your first home by contributing pre-tax earnings into your super fund, up to a $30,000 total limit. The limit in any one year is $15,000. Bear in mind the $25,000 concessional cap may limit how much you can put in, depending on how much you earn, as your 9.5% employer contribution eats into this cap.

These contributions and the earnings they generate are taxed at the favourable rate of 15%.  When you buy your first home, these contributions can be withdrawn to help fund the deposit. In addition, this measure allows you to withdraw an additional amount of your balance calculated at a rate stated by the government, to account for earnings within your fund.

Withdrawals - which can be made any time after 1 July 2018 - will be taxed at 30% below your marginal tax rate. The Treasurer says the boost provided by super over a typical deposit account in this way will accelerate savings by 'at least 30%'. Couples saving for a home can tip in $60,000 jointly into super to reach their deposit goal.

The government gives an example of how the scheme can work:

*Michelle earns $60,000 a year and wants to buy her first home. Using salary sacrifices, she annually directs $10,000 of her pre-tax income into her superannuation account, increasing her balance by $8500 after the contributions tax has been paid by her fund. After three years, she is able to withdraw $27,380 of contributions and deemed earnings on those contributions...After paying $1620 of withdrawal tax she has $25,760 that she can use for her deposit. Michelle has saved around $6240 more for a deposit than if she had saved in a standard deposit account.*

### SUPER INCENTIVE FOR BOOMERS TO DOWNSIZE

At the other end of the housing chain, homeowners aged 65 and over will be incentivised to trade down to a smaller home. The thinking behind this idea is to free up housing stock that can have a knock-on impact right down the chain, by encouraging empty nesters to 'right-size' their home.

If the Budget is passed by the Senate, from 1 July 2018, boomers will be able to make a non-concessional contribution of up to $300,000 from the sale of their principal residence into their superannuation fund, so long as they have lived in their home for at least 10 years.

The downsizing contributions will not count towards the existing non-concessional contribution caps and home-owning couples will be able to take advantage of the measure from the same home to transfer up to $600,000 into super. There's also no requirement to meet the work test.

Other major news announced in the 2017 Budget include:

- Projections to return to surplus in 2020
- Increases in the Medicare Levy
- A major Bank Levy of 0.06% on liabilities for the Big Four plus Macquarie
- Extending the immediate deductibility for small business
- $75 billion of 'good debt' poured into infrastructure over the next decade

## SUPER FIRST HOME ACCOUNTS

First home buyers will be able to use their super to contribute up to $30,000 for a house deposit under the federal government's housing affordability package.

Under the scheme first home buyers will be able to direct $30,000 over and above their compulsory employer contributions, into their super account, specifically for a house deposit.

Those contributions will attract the same tax benefits of super, with contributions and earnings taxed at 15 per cent, rather than marginal rates. Contributions are capped at $15,000 in a single year and cannot include compulsory employer contributions. These contributions count towards your $25,000 concessional cap.

The new rules are proposed to take effect from 1 July 2017 and withdrawals, which will be taxed at 30 per cent below the member's marginal tax rate, will be allowed from 1 July 2018. Money withdrawn must be used to fund a first home deposit.

Mercer Financial Advice Leader Richard Ebbs says the scheme may have the added benefit of engaging more people, particularly younger members, with their super.

"Using an existing structure like super has allowed the Government to avoid creating any extra complexity – and that's definitely a good thing," Ebbs says. "For the vast majority of first home buyers this would be a very suitable method of saving for that all important first home deposit."

He says for couples, both individuals can take advantage of the scheme, bringing potential deposits to $60,000 plus earnings.

If you have already breached the $500,000 limit because of past contributions, no penalty will apply and your past contributions will not be affected.

However this will reduce the amount that you can contribute to your super going forward. Any non-concessional contributions made after 3 May 2016 will be treated as excess and will need to be refunded (with deeming earning taxable) or subject to a non-concessional excess contributions tax.

### FREEING UP THE FAMILY HOME

Older people will be allowed to direct up to $300,000 from the sale of their primary home into super –three times the newly established cap on non-concessional contributions.

If the Budget is passed by the Senate, from 1 July 2018, people aged 65 or over who downsize from a property that has been their main residence for a period of at least 10 years, will be able to make a non-concessional contribution of up to $300,000. These contributions will be in addition to those currently permitted under existing rules and caps, and will be exempt from the work test or the $1.6 million balance test.

Couples selling a jointly owned main residence can contribute up to $600,000 of the proceeds, between them.

The move is part of the Federal Government's attempt to tackle Australia's overheated property market by freeing up established homes and increasing supply.

Mercer Financial Advice Leader Richard Ebbs says the scheme is "an interesting development" but warns retirees to approach it with caution.

"They need to be careful about it because there could be Centrelink implications," Ebbs says. "Your principal place of residence is not counted against the assets test but if you sell it and put it in super, that money is."

"The main benefit of super is that it offers lower tax rates but if you're on the Age Pension you're not paying tax so there's not necessarily much benefit. It might be simpler to invest the money personally."

## TAX CARROT FOR PROPERTY INVESTORS

Individual property investors will be offered more tax incentives to pour money into low cost housing.

If the Budget is passed by the Senate, from 1 January 2018, the capital gains tax discount for individuals investing in "affordable" residential property will increase from 50% to 60%.

To qualify for the extra discount, the housing must be provided to "low or moderate" income tenants and the rate of rent being charged must be at a discount to the market rate.

The affordable rental housing must be managed through a registered community housing provider and the investment held for a minimum of three years.

Mercer Financial Advice Leader Richard Ebbs says the scheme could attract certain investors such as those with a socially responsible ethos, but it's not a simple proposition.

"The extra discount on capital gains is considerable and that might provide added incentive to invest," Ebbs says, "but like any investment you've got to weigh up other factors such as the likely yield, future resale value and whether it complements your other investments."

## HELP HITS WORKERS EARLIER

Thousands of university graduates would be forced to pay off student debts sooner under plans to reduce the HECS/HELP threshold from more than $55,000 to just $42,000.

If the Budget is passed by the Senate, HELP loan repayment thresholds and rates will be set to new levels from 1 July 2018.

At the new low payment threshold of $42,000 a graduate will repay 1% of their income, or $420 per year.

The repayment rate will increase with income, from 1% at the minimum threshold to 10% at $119,882, the maximum threshold; considerably higher than the previous 8% maximum.

Meanwhile all higher education course fees will begin to rise, as the government reduces funding to universities.

Student fees will increase by 1.82% per year for four years, resulting in a total increase in higher education fees of 7.5%.

These fee increases will apply to all students, regardless of when they commenced their study.

## BIG FOUR PLUS MACQUARIE HIT WITH MAJOR LEVY, BUT WHO WILL PAY?

Treasurer Scott Morrison announced a new tax on Australia's big four banks plus Macquarie designed to help towards budget repair. He said the tax was designed to generate a "fair contribution from our major banks, similar to measures imposed in other advanced countries" and would "even up the playing field for smaller banks".

The new tax applies to many of the different types of borrowing that banks use to fund their lending. This includes corporate bonds and deposits over $250,000, but excludes shareholders' capital and smaller deposits even though these are still covered by the Government's guarantee.

If the Budget is passed by the Senate, the new tax will apply from 1 July 2017 to deposit-taking institutions with licensed liabilities of $100bn or more, which scoops up the five major banks. Commonwealth, NAB, ANZ, Westpac and Macquarie will each pay 0.06% of their liabilities in tax. The tax could potentially yield $6 billion over four years.

The new tax is unlike the previous bank deposit tax in that it does not take into account deposits below $250,000. It does not apply to superannuation funds or insurance companies.

The effect of the tax is likely to be reflected in the banks' charges to customers in the form of increased home loans rates, as well as possibly other fees and charges.

## THE PENSIONER CONCESSION CARD AND THE AGE PENSION ELIGIBILITY

The Pensioner Concession Card will be reinstated to those who were no longer eligible for the pension due to the changes to the assets test change introduced on 1 January 2017.

This means that seniors will regain access to State and Territory based concessions that were withdrawn after the change.

People on the age and disability support pensions and parenting payment will also receive one-off cash payments to help cover their winter energy bills — $75 for singles and $125 for couples.

Meanwhile, the government will tighten eligibility for the age pension to foreigners and there are some new rules.

To get the Age Pension, you must have been an Australian Resident, continuously, for 15 years, unless:

• You have had 10 years' continuous Australian residence, with 5 years of this residence between age 16 and Age Pension Age, or

• You have 10 years continuous Australian residence, without having received an activity tested income support payment (mainly Newstart) for a cumulative period of five years.

Depending on your birthdate, from 1 July 2017, the Age Pension age will be 65 years and 6 months. After that, Age Pension age will go up 6 months every 2 years until 1 July 2023 to 67 years of age.

## MEDICARE LEVY

Most tax payers will soon pay higher tax after the government announced an increase in the Medicare Levy to help fund the $22 billion National Disability Insurance Scheme.

The levy is set to increase by 0.5 percentage points — from 2 to 2.5 per cent of taxable income from 1 July 2019.

Other tax rates that are linked to the top personal tax rate, such as the fringe benefits tax rate, will also be increased.
The levy will be reduced for some taxpayers. Income thresholds where the Medicare Levy kicks in will increase, so more people on low incomes will pay no Medicare Levy or a reduced level. These increased thresholds will apply for the current financial year onwards.

| | **2015/16*** | **2016/17 (Proposed)** |
|---|---|---|
| Singles | $21,335 | $21,655 |
| Family | $36,001 plus $3,306 | $36,541 plus $3,356 per child |
| Single Pensioner | $33,738 | $34,244 |
| Family Pensioner | $46,966 plus $3,306 | $47,670 plus $3,356 per child |

*At the time of writing, the 2016/17 rates for Medicare Levy thresholds that would apply under existing legislation have not been announced.

### 1 JULY LEGISLATION RECAP

Superannuation customers will face a raft of new rules from 1 July 2017 after the Federal Government successfully passed a number of its superannuation changes into law.

The tax concessions offered in the super environment remain generous and the final superannuation reform package, approved by the Senate on 23 November 2016, is in-line with the Government's objective of ensuring the superannuation system is fair, flexible and fit for purpose. The Government will legislate to define the primary objective of the superannuation system: "to provide income in retirement to substitute or supplement the Age Pension", whilst providing an "anchor" for future superannuation reforms.

The following summarises the changes in 2017/2018, providing you with an overview of the new rules and some actions to consider, should the new rules affect your super or pension accounts.

## PENSIONS CAPPED AT $1.6 MILLION

From 1 July 2017, there will be a limit on how much of your super you can transfer from your super account in accumulation phase to a tax free pension account. This limit is known as the 'transfer balance cap'.

New and existing pension accounts that support your tax-free retirement income will be counted towards the transfer balance cap.

If you already have more than $1.6m in assets supporting your pension you'll need to remove the excess. If your balance is between $1.6m and $1.7m on 1 July 2017 you'll have until 31 December 2017 to comply with the new rules. If you have more than $1.7m, you'll need to act before 1 July.

You can reduce your pension balance either by rolling the excess amount back into an accumulation account – where you'll pay 15% tax on any earnings – or investing it outside of super – where you'll pay your personal rate (ranging from 0% to 47%) on any earnings.

There is no limit on the amount of money you can have in your normal accumulation super account where earnings are taxed at 15%.

Capital gains tax relief is available if you have to move an asset from pension to accumulation phase in order to satisfy the $1.6 million transfer balance cap.

Whether you choose to roll your additional funds back into your accumulation super account or invest elsewhere depends very much on your personal circumstances – particularly your income outside of super – and is something you should speak to a financial adviser about.

If you start a pension after 1 July 2017, your opening balance will be restricted to $1.6 million. Later investment earnings are not included in the cap so your pension account can grow over time to more than $1.6 million.

Transition pension earnings no longer tax-free

From 1 July, popular transition to retirement (TTR) accounts will lose their tax-free status so earnings will be taxed at 15%, just like a normal super account.

The tax on the income you draw from your TTR will stay the same – your marginal tax rate less 15% if you're under 60 and tax-free if you're over 60 – but the tax on earnings means the argument for a TTR strategy after July 1, 2017 is not as compelling, particularly for those on high incomes and those aged under 60-years.

But if you started a TTR because you wanted to work less hours and supplement your income, or because you needed money to pay down some debt, then it might still be the right for you.

# EXISTING RETIREES WILL HAVE TO BRING THEIR PENSION BALANCES UNDER $1.6 MILLION BEFORE 1 JULY 2017.

Existing pension accounts in excess of $1.6 million will incur penalty tax similar to excess contributions. Existing retirees whose pension account balance(s) will be, or will likely be, more than $1.6 million at 1 July 2017 have the option to either transfer the excess back into an accumulation account or withdraw the excess from super.

The $1.6 million transfer balance cap applies across your total pension assets (which may be held in multiple pension accounts across multiple superannuation funds).

A cancelled pension will pay out previously used cap amounts, allowing a new pension to be commenced without breaching the transfer cap. This allows product switching of pensions, or moving back and forth from super to pension as income needs change.

Speak to your financial adviser who can help you review your options and advise any actions you need to take if your balance is, or will likely be, over $1.6 million.

Five changes to super contributions

Australia's superannuation system is about to undergo its biggest shake up in a decade, including major changes to what you can contribute to your account and how.

These five significant changes will come into effect from 1 July 2017.  Make sure you understand what they mean for you and speak to a Mercer financial adviser to help adapt your contribution strategy.

1. Reduced concessional (before-tax) contributions

The concessional contribution cap for before-tax super contributions – including employer Superannuation Guarantee payments and salary sacrifice – will drop to $25,000 a year for everyone; down from $30,000 for those aged under 50 and $35,000 for those 50 or older.

The change will make it more difficult to boost your super quickly in the years leading up to retirement, so you'll need to start thinking about super earlier in your career.

The new caps don't come into effect until 1 July 2017, so there's still time to take advantage of the existing, more generous limits.

2. Reduced non-concessional (after-tax) contributions

After-tax superannuation caps will drop to $100,000 a year, down from $180,000. Those under age 65 will still be able to "bring forward" three years of after-tax contributions, but the limit will be reduced to $300,000, down from $540,000.

Under the new rules, you won't be able to make any non-concessional contributions once your total super balance reaches $1.6 million.

Again, the new caps don't come into effect until 1 July 2017 so there may still be time to take advantage of the existing, more generous limits.

3. Spouse contributions more widely available

The spouse tax offset will be extended to more couples. Before 1 July, 2017, a tax offset of up to $540 is available for individuals who make superannuation contributions to their spouse's account – if their spouse's total income is less than $13,800.

Under the new rules the offset will be extended to those whose recipient spouses earn up to $40,000.  The offset gradually reduces for incomes above $37,000 and completely phases out at incomes above $40,000.

The move means there is greater flexibility to support your partner and include spouse contributions as part of your overall strategy.

4. Widening access to concessional contributions

All individuals under the age of 65, and those aged 65 to 74 who meet the work test, will be able to claim a tax deduction for personal contributions to eligible superannuation funds up to the concessional contributions cap.

An income tax deduction for personal superannuation contributions before 1 July 2017 is only available to people who earn less than 10 per cent of their income from salary or wages.

5. Introducing catch up contributions

From 1 July 2018, super customers will be able to “carry forward” any unused concessional cap amounts for up to five financial years. This change will apply to people with total super balances of less than $500,000.

Unused amounts “carried forward” can only be used in subsequent years, so the first year in which you’ll be able to access the ability to contribute more than the normal cap is 2019–20.

Catch up contributions could be helpful for those who take time out of work, whose income varies considerably from one year to the next, or whose circumstances have changed and are now in a position to increase their contributions to superannuation.

## NOW IS THE TIME TO ACT

Contribution caps are about to be slashed but current rules apply until 30 June 2017, providing an opportunity to increase your before-tax contributions. So if you have been thinking about putting more money into super, it’s time to act.

Before 1 July:

- Before-tax contribution caps are $30,000 a year for those under 50 and $35,000 a year for those 50 plus
- After-tax contribution caps are $180,000 a year
- The three-year bring-forward rule on after-tax contribution is $540,000 for those under the age of 65