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HOUSE OF REPRESENTATIVES

TREASURY LAWS AMENDMENT (FAIR AND SUSTAINABLE SUPERANNUATION) BILL 2016

EXPOSURE DRAFT EXPLANATORY MATERIALS

DRAFT

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Glossary

The following abbreviations, acronyms and concepts are used throughout this explanatory memorandum.

Abbreviation	***Definition***
Accumulation phase	The period during which a superannuation interest is not in the retirement phase
APRA	Australian Prudential Regulation Authority
AWOTE	Average Weekly Ordinary Time Earnings
Capped defined benefit balance	The net amount of capital an individual has transferred to their superannuation retirement phase to support capped defined benefit income streams
CGT	Capital Gains Tax
Commissioner	Commissioner of Taxation
Commutation	The process of ceasing, in whole or in part, a superannuation income stream and converting it into a superannuation lump sum
CPI	The Consumer Price Index
Debit value	The residual component of a capped defined benefit income stream's special value
Deferred superannuation income stream	To be defined in related regulations. Will include guaranteed annuities and group self-annuities where a superannuation income stream benefit payment is delayed
Defined benefit income cap	The amount of superannuation income stream benefits an individual can receive from capped defined benefit income streams before being subject to additional income tax – $100,000 in 2017-18 and indexed to the general transfer balance cap
Division 293	Division 293 of the *Income Tax Assessment Act 1997*
Excess transfer balance	The amount by which an individual's transfer balance account exceeds the their personal transfer balance cap on a particular day (unless the excess is attributable to the individual's capped defined benefit balance)

Abbreviation	***Definition***
Excess transfer balance tax	Tax imposed on notional earnings over a financial year
General transfer balance cap	An amount, $1.6 million in 2017-18 and indexed to the CPI in $100,000 increments
ITAA 1997	*Income Tax Assessment Act 1997*
ITAR 1997	*Income Tax Assessment Regulations 1997*
IT(TP)A 1997	*Income Tax (Transitional Provisions) Act 1997*
Notional earnings	An amount in respect of an excess transfer balance for a particular day, generally credited to an individual's transfer balance account
PAYG Withholding	Pay-As-You-Go Withholding
Personal transfer balance cap	The maximum amount of capital an individual can transfer to their superannuation retirement phase, indexed proportionally to the general transfer balance cap
RP or Retirement phase	The period during which a superannuation income stream is currently payable, or, if it is a deferred superannuation income stream, when a person has met a relevant nil condition of release. A TRIS is never in the retirement phase
Reversionary income stream	A superannuation income stream that automatically reverts to a nominated beneficiary on the death of its current recipient
RSA	Retirement Savings Account
RSAR 1997	*Retirement Savings Accounts Regulations 1997*
SISR 1994	*Superannuation Industry (Supervision) Regulations 1994*
SMSF	Self-managed superannuation fund
Special value	The modified starting value of a capped defined benefit income stream

Abbreviation	***Definition***
Superannuation death benefit	A superannuation lump sum, superannuation income stream or superannuation income stream benefit a person receives because of the death of another person
Superannuation income stream	Generally a right to receive periodic payments from a superannuation interest, for example a pension or annuity
Superannuation income stream benefit	Each individual payment an individual receives under a superannuation income stream
Superannuation lump sum	A benefit (other than a superannuation income stream benefit) an individual receives from a superannuation interest
TAA 1953	*Taxation Administration Act 1953*
Total superannuation balance	A method for valuing all of an individual’s superannuation interests.
Transfer balance account	The net amount of capital an individual has transferred to their superannuation retirement phase
TRIP	Transition to retirement income pension
TRIS	Transition to retirement income stream (generally also includes transition to retirement income pensions, non-commutable allocated annuities and non-commutable allocated pensions)

Chapter 1
Transfer balance cap

Outline of chapter

1.1 The exposure draft of Schedule 1 to the Treasury Laws Amendment (Fairer and Sustainable Superannuation) Bill 2016 (the Bill) imposes a $1.6 million cap (the transfer balance cap) on the amount of capital that can be transferred to the retirement phase of superannuation from 1 July 2017. This cap is intended to limit the extent to which the tax-free benefits of retirement phase accounts can be used by high wealth individuals.

1.2 Schedule 1 also imposes additional income tax rules on recipients of defined benefit pensions in excess of $100,000 to achieve a commensurate outcome.

Context of amendments

1.3 This measure forms part of the Government's Superannuation Reform Package announced in the 2016-17 Budget. The measure improves the sustainability and equity of the superannuation system.

1.4 Individuals' investments in superannuation are generally subject to a concessional earnings tax rate of 15 per cent. The tax is imposed on the individual's superannuation fund. Members benefit through higher after-tax returns. This rate generally applies while the individual is of working age and contributing towards their superannuation (the accumulation phase).

1.5 When an individual accesses their superannuation (for example, because they have retired), they may take superannuation in the form of a superannuation lump sum or a superannuation income stream such as a pension, or a combination of the two. If they commence a superannuation income stream, income earned on the ongoing investment of the capital amount benefits from an earnings tax exemption. This exemption applies to the fund for the benefit of members. Individuals in receipt of a superannuation income stream, and the assets supporting those income streams, are said to be in the retirement phase or pension phase.

1.6 The purpose of the earnings tax exemption is to encourage individuals to save for their own retirement and relieve pressure on Australia's Age Pension system. However, there is currently no limit to the amount of superannuation an individual can move into the retirement phase where it benefits from the tax exemption. As such, the exemption provides a significant tax concession to high wealth individuals with significant superannuation balances and who will almost certainly never be reliant on the age pension. The amendments made by Schedule 1 ensure the superannuation tax concessions are better targeted and reduce the extent to which superannuation is used for tax minimisation and estate planning.

Operation of the existing law

The earnings tax exemption

1.7 The earnings tax exemption is provided for in sections 295-385 and 295-390 of the *Income Tax Assessment Act 1997* (ITAA 1997). Those provisions broadly exempt income that a superannuation fund receives in respect of assets it holds to fund its liabilities to provide superannuation income stream benefits to its members.

1.8 A superannuation income stream is an individual's right to receive a series of periodic payments over an identifiable period of time. This includes pensions and annuities. A superannuation income stream benefit is any one of those periodic payments (section 307-70 of the ITAA 1997 and regulation 995-1.01 of the *Income Tax Assessment Regulations 1997*).

1.9 Funds can segregate the assets they hold that support superannuation income stream benefit liabilities, with earnings on segregated assets exempt from tax. Alternatively, where assets are not held solely to fund pension liabilities, funds are required to use the proportional method, where a proportion of earnings on all of a fund's assets are exempt.

1.10 Life insurance companies and Retirement Savings Account (RSA) providers can also have liabilities in relation to superannuation income stream benefits. However, in most cases, the exemptions that apply to those entities use related concepts.

1.11 The earnings tax exemption is discussed in more detail in Chapter 8.

Taxation of superannuation income stream benefits

1.12 Most superannuation income stream member benefits are non-assessable non-exempt income to individuals aged 60 or over (section 301-10 of the ITAA 1997). This is because they are wholly from a taxed source (or 'element taxed in the fund') (subsection 307-275(2) of the ITAA 1997).

1.13 A number of superannuation funds provide benefits that contain untaxed elements. These include constitutionally protected funds (section 307-280 of the ITAA 1997) and some public sector defined benefit schemes (section 307-295 of the ITAA 1997). Where the benefit is from an untaxed source, the benefit is assessable to the individual, subject to a 10 per cent tax offset (section 301-100 of the ITAA 1997).

1.14 Similar rules to the above apply in the case of superannuation income stream benefits that are superannuation death benefits paid to dependants. The difference is that the treatment for individuals aged 60 or over (who receive member benefits) is replicated for a younger person if their superannuation death benefits are from a deceased person who was aged 60 or over (Subdivision 302-B of the ITAA 1997).

Summary of new law

1.15 Schedule 1 to the Bill imposes a transfer balance cap from 1 July 2017 to limit the amount of capital individuals can transfer to the retirement phase to support superannuation income streams. This, in turn, limits the amount of earnings that are exempt from taxation.

1.16 An individual's transfer balance cap is $1.6 million for the 2017-18 financial year and is subject to proportional indexation on an annual basis in line with the Consumer Price Index (CPI).

1.17 The value of superannuation interests that support superannuation income streams as at 30 June 2017, together with the commencement value of new superannuation income streams that start after that date, count towards an individual's cap.

1.18 If an individual breaches their transfer balance cap, the Commissioner of Taxation (the Commissioner) will direct an individual's superannuation income stream provider to commute (reduce) their retirement phase interests by the amount of the excess (including notional earnings on the excess) to rectify the breach. The individual will also be liable for excess transfer balance tax on their notional earnings to neutralise the benefit received from having excess capital in the tax free

retirement phase. The tax rate on notional earnings increases for second and subsequent breaches.

1.19 Child dependants that receive a superannuation income stream from a deceased parent are subject to modifications. The modifications generally allow the child to receive their share of the deceased's retirement assets without prejudice to the child's future retirement. This recognises that most child dependants are currently required to commute the superannuation income streams by age 25.

1.20 Defined benefit lifetime pensions and certain other superannuation income streams subject to commutation restrictions are subject to commensurate taxation treatment. An equivalent outcome to the operation of the transfer balance cap is achieved, albeit in a different manner, recognising that commutation restrictions make it impractical for individuals to reduce an excess amount.

1.21 The value of lifetime pensions and other defined benefit income streams is counted towards an individual's transfer balance cap. Excess transfer balance tax is not imposed for a breach of the transfer balance cap that is attributable to certain defined benefit income streams. Excess defined benefit income is instead subject to additional income tax rules.

1.22 Transitional arrangements apply to individuals receiving superannuation income streams on 1 July 2017. These arrangements only apply if the individual is in breach by less than $100,000 on 1 July 2017.

1.23 Transitional provisions provide Capital Gains Tax (CGT) relief. Superannuation providers are able to reset the cost base of assets reallocated from the retirement phase to the accumulation phase prior to 1 July 2017. This relief is available for providers in respect of the assets held for individuals who choose to transfer amounts from the retirement phase to the accumulation phase to comply with the transfer balance cap or new transition to retirement income stream (TRIS) arrangements.

1.24 Where these assets are already partially supporting accounts in the accumulation phase (a non-segregated fund), tax will be paid on this proportion of the capital gain made prior to 1 July 2017. This tax may be deferred until the asset is sold, for up to 10 years.

Comparison of key features of new law and current law

New law	*Current law*
Limit the amount an individual can transfer to the retirement phase of superannuation where it is subject to the earnings tax exemption	
The fund earnings tax exemption is generally retained. However, individuals are required to limit transfers to the retirement phase to $1.6 million (indexed). Individuals that breach the transfer balance cap will have their superannuation income streams commuted (in full or in part) back to the accumulation phase and will be subject to excess transfer balance tax.	A superannuation fund is exempt from tax in relation to earnings on assets that support a pension liability. Individuals receiving pensions benefit from the exemption in the form of higher after-tax returns. There is no limit to the amount of superannuation an individual can move into retirement phase where it is subject to the exemption.
Include half of the defined benefit income in a recipient's assessable income to the extent it exceeds a $100,000 defined benefit income cap	
In taxed defined benefit arrangements, half of the capped defined benefit income stream payments are included in the recipient’s assessable income and taxed at the individual’s marginal rates to the extent they exceed a defined benefit income cap of $100,000 (indexed).	Superannuation income stream benefits (member benefits) from taxed sources are non-assessable non-exempt income to recipients aged 60 or over. Superannuation income stream benefits that are dependant death benefit payments from taxed sources are also non-assessable non-exempt income if the deceased was 60 or over.
Limit the defined benefit income from untaxed sources that can attract a tax offset to the defined benefit income cap	
In untaxed defined benefit arrangements, the tax offset is limited to the first $100,000 (indexed) of defined benefit income the individual receives. Defined benefit income received in excess of the defined benefit income cap does not attract the offset.	Member benefits from untaxed sources are assessable income to recipients but recipients aged 60 or over are entitled to a 10 per cent tax offset. Superannuation income stream benefits that are dependant death benefit payments from untaxed sources are also entitled to a 10 per cent tax offset if the deceased was 60 or over.

New law	*Current law*
Adjustments to the defined benefit income cap for other defined benefit income	
Other superannuation income stream member benefits and dependant death benefits remain subject to their existing tax treatment. However, if the other benefits are defined benefit income, the defined benefit income cap is reduced by the amount of that income.	Other superannuation income stream member benefits and dependant death benefits are subject to a variety of different tax treatments. Concessions for these types of income are generally limited.
Allow complying superannuation funds reallocating assets from retirement phase to the accumulation phase before 1 July 2017 to reset their cost base	
Complying superannuation funds are able to reset the cost base of assets that are reallocated from the retirement phase to the accumulation phase prior to 1 July 2017. Where these assets are already partially supporting accounts in the accumulation phase, tax will be paid on this proportion of the capital gain made to 1 July 2017. This tax may be deferred until the asset is sold, for up to 10 years.	Where fund assets are segregated, movements between the pension and accumulation pool have no bearing on the cost base of the asset. For funds that are not segregated, gains on assets used to support accounts in the accumulation are included in the assessable income of the fund on realisation under the CGT provisions and using a proportional method.

Detailed explanation of new law

1.25 The transfer balance cap is designed to limit the amount of capital that an individual can transfer to the retirement phase of superannuation. Unlike other balance tests in the exposure draft, the transfer balance cap does not require an annual revaluation of superannuation assets. The transfer balance cap is directed towards net transfers to the retirement phase and does not value earnings, losses or draw-downs that occur within the retirement phase. ***[Schedule 1, Part 1, item 3, sections 294-1 and 294-5 of the ITAA 1997]***

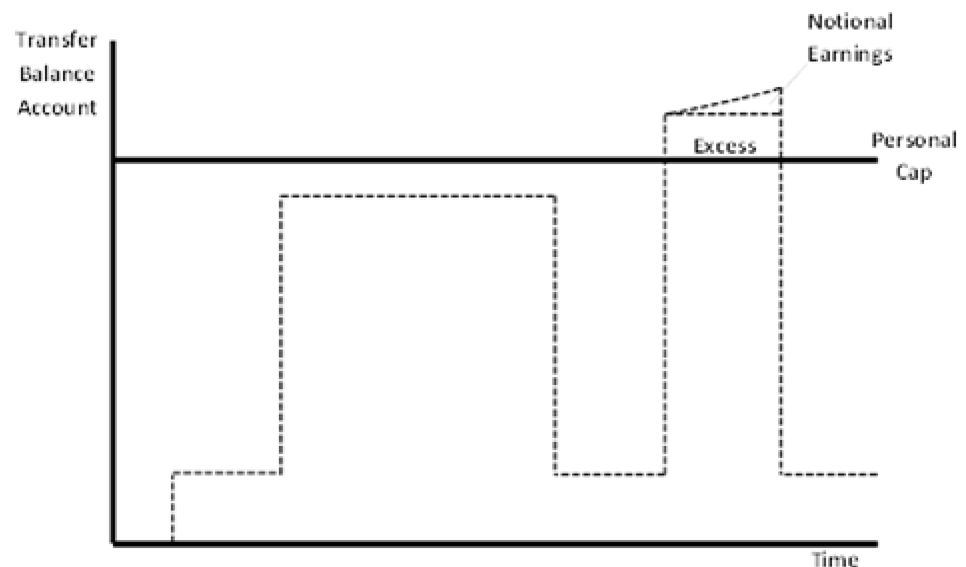
1.26 Each individual will have a personal transfer balance cap reflecting the total amount they can transfer to the retirement phase. To determine an individual's position with respect to their transfer balance cap, each individual will have a transfer balance account, which tracks the net amounts the individual has transferred to the retirement phase. ***[Schedule 1, Part 1, item 3, section 294-10 and subsection 294-15(1) of the ITAA 1997]***

The transfer balance account

1.27 The transfer balance account operates in a similar way to a bank account statement balance or the balance of a general account ledger. Amounts an individual transfers to the retirement phase give rise to a credit in their transfer balance account. Similarly, certain transfers out of the retirement phase give rise to a debit in the individual's transfer balance account.

1.28 An individual breaches their transfer balance cap if their transfer balance account exceeds their personal transfer balance cap. Notional earnings accrue on the excess balance and are credited to the balance, compounding the excess until it is rectified.

Diagram 1.1: Transfer balance account credits, debits and excess amounts



1.29 It is possible for an individual's transfer balance account to have a negative balance if their debits exceed their credits (see Example 1.7).

1.30 An individual's transfer balance account is created when credits first arise in the account. This is when they first receive a superannuation income stream that is in the retirement phase. ***[Schedule 1, Part 1, item 3, subsection 294-15(2) of the ITAA 1997]***

1.31 As noted above, the colloquial concept of the retirement phase of superannuation is not new. However, the concept is now incorporated into the taxation law and is relevant to superannuation providers' earnings tax exemptions (see Chapter 8).

1.32 An individual generally starts to be a recipient of a retirement phase superannuation income stream when they start a superannuation income stream and superannuation income stream benefits are payable to them. ***[Schedule 1, Part 1, item 3, subsection 294-20(1) of the ITAA 1997]***

1.33 For individuals that are receiving retirement phase superannuation income streams at 1 July 2017, their transfer balance account begins on that date. ***[Schedule 1, Part 1, item 3, paragraph 294-15(2)(a) of the ITAA 1997]***

1.34 For individuals with deferred superannuation income streams, it is not necessary that benefits are currently payable to the individual. It is sufficient that the benefits will become payable. ***[Schedule 1, Part 1, item 3, subsection 294-20(2) of the ITAA 1997]***

1.35 An individual's transfer balance account is generally a lifetime account and only ceases on their death. However, a modification applies to cease a child's account that is created when a child starts to receive a superannuation income stream because they receive a superannuation death benefit (see paragraphs 1.205 to 1.220). The child may then start a normal transfer balance account when they retire.

The transfer balance cap

1.36 The general transfer balance cap is $1.6 million for the 2017-18 financial year and is subject to indexation on an annual basis in line with CPI. ***[Schedule 1, Part 1, item 3, subsection 294-35(3) of the ITAA 1997]***

1.37 An individual's personal transfer balance cap equals the general transfer balance cap for the financial year in which they first have a transfer balance account.

Example 1.1: Starting a personal transfer balance cap

Amy first becomes entitled to superannuation income stream benefits in 2017-18. A transfer balance account is created for Amy at that time. Amy's personal transfer balance cap is $1.6 million for the 2017-18 financial year.

Allen first becomes entitled to superannuation income stream benefits in 2021-22. A transfer balance account is created for Allen at that time. In 2021-22, the general transfer balance cap has indexed to

$1.7 million. Allen's personal transfer balance cap is $1.7 million for the 2021-22 financial year.

Proportional indexation of the personal transfer balance cap

1.38 Where an individual starts to have a transfer balance account and has not used the full amount of their cap, their personal transfer balance cap is subject to proportional indexation. ***[Schedule 1, Part 1, item 3, subsections 294-35(1)and (2) of the ITAA 1997]***

1.39 Each individual's personal transfer balance cap is indexed proportionally in line with increases in the general transfer balance cap. ***[Schedule 1, Part 1, item 3, subsection 294-35(2) of the ITAA 1997]***

1.40 Proportional indexation is intended to hold constant the proportion of an individual's used and unused cap space as their personal cap increases. An individual's personal cap is only indexed by their unused cap percentage. This is worked out by finding the individual's highest transfer balance, comparing it to their personal transfer balance cap on that day and expressing the unused cap space as a percentage. Once a proportion of cap space is utilised, it is not subject to indexation, even if the individual subsequently removes capital from their retirement phase. ***[Schedule 1, Part 1, item 3, section 294-40 of the ITAA 1997]***

1.41 The purpose of proportional indexation is to provide equitable treatment to all individuals over time. It also recognises the expected benefit gained by individuals from commencing a retirement phase account at an earlier time.

Example 1.2: Proportional indexation

Further to Example 1.1, Amy's transfer balance account is credited by $800,000 in 2017-18. At that time, she has used 50 per cent of her $1.6 million personal transfer balance cap.

When the general transfer balance cap is indexed to $1.7 million in 2020-21, Amy's personal transfer balance cap is increased proportionally to $1.65 million. That is, Amy's personal transfer balance cap is increased by 50 per cent of the corresponding increase to the general transfer balance cap. As such, Amy can now contribute $850,000 without breaching her personal cap.

Example 1.3: Proportional indexation and the highest balance

On 1 October 2017, Nina commences a superannuation income stream of $1.2 million. On 1 January 2018 Nina partially commutes her superannuation income stream by $400,000 to buy an investment property.

Nina's transfer balance account on 1 October 2017 was $1.2 million and, on 1 January 2018, it is $800,000 (Nina's account is debited in respect of the $400,000 partial commutation, see paragraphs 1.64 to 1.74).

In 2020-21, the general transfer cap is indexed to $1.7 million. To work out the amount by which her personal cap is indexed Nina identifies the highest balance in her transfer balance account ($1.2 million), the day on which she first started to have this balance (1 October 2017), and her personal cap on that date ($1.6 million). Therefore Nina's unused cap percentage on 1 October 2017 is 25 per cent.

To work out how much her personal cap is indexed, Nina applies her unused cap percentage to the amount by which the general cap has indexed $100,000 (the indexation increase). Therefore Nina's personal transfer balance cap in 2020-21 is $1,625,000.

In 2022-23, the general transfer balance cap is indexed to $1.8 million. As Nina hasn't transferred any further amount into retirement phase her unused cap percentage remains 25 per cent. Her personal transfer balance cap is now $1.65 million (25 per cent of the indexation increase of $100,000).

In this year, Nina decides to transfer the maximum amount she can into the retirement phase. This will be her personal cap for the 2022-23 year ($1,650,000) less her transfer balance account $800,000. This means Nina can transfer another $850,000 into the retirement phase without exceeding her transfer balance cap.

1.42 An individual that has exhausted or exceeded their transfer balance cap will not have their personal cap indexed.

1.43 A modified transfer balance cap applies to a child dependant that receives a death benefit income stream from a deceased person (see paragraphs 1.205 to 1.220). The above rules do not apply to these transfer balance caps.

Indexation of the general transfer balance cap

1.44 New indexation rules are inserted into the ITAA 1997 to provide a framework for indexing amounts in increments. ***[Schedule 1, Part1, item 8, section 960-290 of the ITAA 1997]***

1.45 The general transfer cap will be indexed in $100,000 increments in line with CPI. ***[Schedule 1, Part 1, item 8, item 1 in the table in subsection 960-290(6) of the ITAA 1997]***

1.46 The general transfer balance cap is indexed by being multiplied by the indexation factor and rounding down to the nearest $100,000. The

indexation factor is determined by dividing the CPI number for the quarter ending 31 December in the prior financial year by the number for the base quarter (31 December 2016).

1.47 The general transfer balance cap does not increase where the indexation factor is one or less than one.

Credits to an individual's transfer balance account

1.48 Generally, a credit arises in an individual's transfer balance account when an individual becomes the recipient of a superannuation income stream that is in the retirement phase. That time is when the superannuation income stream begins to attract an earnings tax exemption for the superannuation income stream provider.

1.49 The following amounts are credited towards an individual's transfer balance account:

- the value of all superannuation interests that support superannuation income streams in the retirement phase the individual is receiving on 30 June 2017;
- the commencement value of new superannuation income streams (including new superannuation death benefit income streams and deferred superannuation income streams) in the retirement phase that start after that date;
- the value of reversionary superannuation income streams at the time the individual becomes entitled to them; and
- notional earnings that accrue on excess transfer balance amounts.

[Schedule 1, Part 1, item 3, subsection 294-25(1) of the ITAA 1997]

1.50 Changes to the value of a superannuation interest that supports a superannuation income stream after the initial valuation that credits the individual's transfer balance account are not taken into consideration. That means a superannuation interest that supports a superannuation income stream that increases in value because of investment earnings does not have its growth counted towards the cap. Similarly, a superannuation interest that supports a superannuation income stream that loses value because of investment losses or the periodic drawdown of superannuation income stream benefits does not have that reduction reflected in the individual's transfer balance account.

Example 1.4: Transfer balance account credits

On 1 August 2017, John starts a pension worth $1 million. At 1 July 2018, the value of the superannuation interest that supports John's pension has grown to $1.1 million because of investment earnings. By 1 January 2030, John has drawn-down the full value of the superannuation interest that supported his pension.

At all times, John has a transfer balance account of $1 million reflecting the credit that arose on 1 August 2017.

1.51 Modifications apply to working out the amount of credits that arise in relation to capped defined benefit income streams (see paragraphs 1.157 to 1.186)

Modifications for reversionary superannuation income streams

1.52 A new beneficiary becomes the recipient of a reversionary superannuation income stream on the death of the previous beneficiary. The credit that arises in respect of the superannuation income stream is the value of the supporting superannuation interest at the time of the deceased's death. This is consistent with the general rules outlined above.

1.53 A modification applies to defer the time the credit arises in the new beneficiary's transfer balance account. The deferred time is six months after the beneficiary first receives the reversionary superannuation income stream. This gives the new beneficiary sufficient time to adjust their affairs following the death of a relative before any consequences – for example, a breach of their transfer balance cap – arise. ***[Schedule 1, Part 1, item 3, paragraph (b) of column 3 in items 1 and 2 in the table in subsection 294-25(1) of the ITAA 1997]***

Example 1.5: Credits for reversionary superannuation income streams

John has a reversionary pension worth $1 million at the time of his death on 1 August 2017. The pension reverts to John's wife, Heather. Heather already has her own pension and a transfer balance account with a balance of $800,000.

In November 2017, Heather is advised that, in August, she became the recipient of John's pension. Heather is advised that, unless she acts, the combined value of the two pensions will cause her to breach her transfer balance cap. Heather has a number of options to respond to the situation. She can fully commute either pension or she can undertake a partial commutation for the amount of the potential excess, $200,000.

On 1 December 2017, Heather makes a partial commutation of her pension and receives a superannuation lump sum of $200,000. On that date, a debit arises in her transfer balance for that amount (see

paragraphs 1.64 to 1.74) bringing her transfer balance account down to $600,000.

The $1 million credit in respect of the reversionary pension arises in Heather's transfer balance account on 1 February 2018. Heather has not breached her transfer balance cap.

Notional earnings on excess transfer balances

1.54 An excess transfer balance arises when an individual's transfer balance account exceeds their personal transfer balance cap on a particular day. ***[Schedule 1, Part 1, item 3, section 294-30 of the ITAA 1997]***

1.55 Notional earnings accrue on excess transfer balances. Notional earnings accrue daily and are generally credited towards an individual's transfer balance account. This means notional earnings compound daily until the breach of the transfer balance cap is rectified or the Commissioner issues a determination. ***[Schedule 1, Part 1, item 3, item 3 in the table in subsection 294-25(1) and subsection 294-220(1) of the ITAA 1997]***

1.56 The rate at which notional earnings accrue is based on the general interest change. ***[Schedule 1, Part 1, item 3, subsection 294-220(2) of the ITAA 1997]***

1.57 The daily rate is worked out as follows:

$$\frac{\mathbf{90}\ \mathit{Day\ Bank\ Accepted\ Bill\ yield} + \mathbf{7}\ \mathit{percentage\ points}}{\mathit{The\ number\ of\ days\ in\ the\ year}}$$

1.58 The 90-day Bank Accepted Bill yield is the benchmark indicator for short-term interest rates. For example, during the 2015-16 financial year, the general interest charge averaged 9.2 per cent per annum. The indicator is published by the Reserve Bank of Australia.

1.59 A treasury portfolio minister may vary the daily rate downwards by legislative instrument. ***[Schedule 1, Part 1, item 1, subsections 294-220(2) and (3) of the ITAA 1997]***

Example 1.6: Notional Earnings

Andrew has a personal transfer balance cap of $1.6 million. His self-managed superannuation fund (SMSF) starts a pension for Andrew worth $2 million. On that day, Andrew has an excess transfer balance of $400,000. Andrew realises his mistake 30 days later and decides to make a partial commutation of the pension to remove the excess.

Over the course of the 30-day period, Andrew's transfer balance account was credited with notional earnings of $3,036 (all examples in

this Chapter assume an annual rate of 9.2 per cent). This brought Andrew's transfer balance account up to $2,003,036.

Andrew calculates his excess transfer balance at the end of the 30-day period and, on that day, makes a partial commutation in return for a superannuation lump sum of $403,036. Andrew receives a debit for that amount in his transfer balance account (see paragraphs 1.64 to 1.74). This brings his transfer balance account back in line with the $1.6 million transfer balance cap. Andrew cannot make any further contributions to his retirement phase account.

1.60 Notional earnings continue to accrue but are no longer credited to an individual's transfer balance account once the Commissioner has issued a transfer balance determination (see paragraphs 1.101 to 1.108). This means the notional earnings that arise during this period do not contribute to an individual's excess and do not compound. This allows the Commissioner's determination to identify a fixed excess transfer balance that must be removed from the retirement phase. ***[Schedule 1, Part 1, item 1, subsection 294-25(2) of the ITAA 1997]***

1.61 Excess transfer balance tax is payable on accrued amounts of notional earnings whether or not those amounts have been credited to, or debited from, an individual's transfer balance account. Excess transfer balance tax is assessed for a financial year during which an individual was in breach of their transfer balance cap (see paragraphs 1.148 to 1.156).

1.62 An excess transfer balance is disregarded if it is less than $100,000; is caused by existing superannuation income streams on 1 July 2017; and the individual rectifies the breach within 60 days (see the discussion of transitional provisions at paragraphs 1.266 to 1.268).

1.63 Capped defined benefit income streams do not give rise to an excess transfer balance and are not subject to excess transfer balance tax. Commensurate income tax treatment applies in relation to capped defined benefit income streams (see paragraphs 1.157 to 1.186).

Transfer balance account debits

1.64 An individual's transfer balance account is debited when they commute capital from the retirement phase of superannuation. This facilitates roll-overs and ensures that an individual's transfer balance account reflects the net amount of capital an individual has transferred to the retirement phase of superannuation. An individual's transfer balance account also receives a debit for certain other events that reduce the value of the individual's retirement phase assets. ***[Schedule 1, Part 1, item 3, section 294-65 of the ITAA 1997]***

1.65 Superannuation income stream benefit payments that reduce the value of a superannuation interest that supports a superannuation income stream are not debited from the individual's transfer balance account. This reflects the expectation that, once an individual has utilised their cap, the value of the individual's retirement-phase assets will eventually decline as the individual uses this income to support themselves in their retirement. This ensures the benefit of the retirement phase earnings exemption is limited appropriately to support individuals during their retirement.

1.66 Just as investment gains are not credited towards an individual's transfer balance account, investment losses do not give rise to debits.

1.67 The following section describes the general rules for debiting the transfer balance account. Modifications apply to debits in relation to capped defined benefit income streams (see paragraphs 1.173 to 1.183).

Debits for commutations

1.68 A superannuation income stream may be reduced by commuting it into a superannuation lump sum. A superannuation lump sum arising from a commuted superannuation income stream may be retained in the superannuation system. Retained superannuation lump sums are treated as being held in the accumulation phase and are subject to concessional earnings taxation of 15 per cent. Alternatively, a superannuation lump sum may be paid outside the superannuation system to the individual personally.

1.69 An individual that commutes a superannuation income stream is generally entitled to debit the value of the superannuation lump sum from their transfer balance account. The debit is applied regardless of whether the commutation amount is retained within the superannuation system or is paid out. ***[Schedule 1, Part 1, item 1, item 3 in the table in subsection 294-70(1) of the ITAA 1997]***

1.70 Because the debit reflects the value by which the superannuation interest that supports the superannuation income stream has been converted to a superannuation lump sum, the amount of a debit applied for a full commutation may exceed the balance of the individual's transfer balance account (or even their transfer balance cap). This effectively allows an individual to start a new superannuation income stream up to the value of the fully commuted superannuation income stream without breaching their transfer balance cap. This ensures an individual who rolls-over their superannuation income stream has the same transfer balance account position as if they had not performed the roll-over.

Example 1.7: Commutation debits

> On 1 July 2017, Taylor purchases a pension worth $1.6 million. On 1 June 2018, the superannuation interest that supports the pension is valued at $1.7 million because of investment earnings. Taylor fully commutes the pension on this day and receives a $1.7 million superannuation lump sum. Taylor debits his transfer balance account by $1.7 million to reach a transfer balance account of –$100,000. Taylor is entitled to start a new pension worth up to $1.7 million without breaching his transfer balance cap.

1.71 An individual may also make a partial commutation of a superannuation income stream. A partial commutation is recognised in the same way. The individual receives a debit for the value of the superannuation lump sum they receive.

Partial commutations and minimum draw-down requirements

1.72 To facilitate the ability for individuals to make partial commutations and receive a debit for the full value of that commutation against their transfer balance account, consequential amendments will be made to the SISR 1994 and RSAR 1997. These amendments will ensure that partial commutations cannot be counted towards the minimum annual payment requirement for superannuation income streams.

1.73 This ensures consistency with the objective of superannuation, which is to provide income to support retirement, and ensures that the benefit of the retirement phase earnings exemption is limited appropriately. Without this change, individuals who had reached their transfer balance cap would be able to cycle their minimum superannuation income stream benefits back into their superannuation income stream without breaching the cap. This is inconsistent with the object of the minimum drawn down requirements.

1.74 The Government will undertake an additional consultation process in relation to these amendments to the regulations.

Structured settlement debits

1.75 A debit also arises with respect to a structured settlement an individual receives and contributes towards their superannuation interests. A structured settlement is a payment for a personal injury the individual has suffered and is defined in section 292-95 of the ITAA 1997 in the context of the excess non-concessional contributions regime. ***[Schedule 1, Part 1, item 3, item 2 in the table in subsection 294-70(1) of the ITAA 1997]***

1.76 The personal injury payment must be in the form of a structured settlement, an order for a personal injury payment or lump sum workers

compensation payment. Two legally qualified medical practitioners must certify that the individual is unlikely to ever be able to be gainfully employed in a capacity for which they are reasonably qualified as a result of the injury.

1.77 Subject to the modification in paragraph 1.78, the contribution must be made to a superannuation fund within 90 days of the payment being received or the structured settlement or order coming into effect, whichever is later. The individual must notify the superannuation provider that the contribution is being made under this exemption before, or when, making the contribution.

1.78 A modification applies to structured settlements an individual received before the start of the excess non-concessional contributions regime on 10 May 2006. These rules remove the requirement that the individual make the contribution within 90 days and the requirement that the individual notify their superannuation provider. This reflects that it was not necessary to comply with these requirements before the start of the excess non-concessional contributions regime. ***[Schedule 1, Part 1, item 3, subsection 294-70(2) of the ITAA 1997]***

1.79 The debit arises when the individual makes the contribution of the structured settlement amount or the time the individual first has a transfer balance account. The debit that arises is the value of the contribution. It is not necessary to link the contribution to any particular amount of capital in the retirement phase.

Example 1.8: Structured settlements

On 13 November 2018, Alice, 42, is seriously injured in a car accident. She undertakes legal proceedings against the driver and is awarded a court ordered structured settlement of $4 million due to the severity of her injuries.

Alice contributes the $4 million into her superannuation fund and immediately commences a superannuation income stream with the amount, notifying the fund and the Commissioner of this contribution. A credit and a debit of $4 million arise in her transfer balance account simultaneously. Alice's transfer balance account is now nil. Alice is entitled to start another pension worth up to $1.6 million without breaching her transfer balance cap.

Replenishment debits

1.80 There are a limited number of events that may result in an individual losing some or all of the value in their superannuation interests. These include family law payment splits, fraud and void transactions under the *Bankruptcy Act 1966*. In these specific circumstances, an

affected individual is able to notify the Commissioner of the event and receive a debit in their transfer balance account. There is no time limit within which the Commissioner needs to be notified. ***[Schedule 1, Part 1, item 3, items 3 and 4 in the table in subsection 294-70(1), and sections 294-75 and 294-80 of the ITAA 1997]***

Fraud

1.81 Where the superannuation interest that supports an individual's superannuation income stream is reduced because of a loss suffered by the superannuation income stream provider as a result of fraud or dishonesty, and the offender is convicted, the individual is able to notify the Commissioner and receive a debit in their transfer balance account to the value of the reduction. ***[Schedule 1, Part 1, item 3, item 3 in the table in subsection 294-70(1) and subsections 295-75(2) to (4) of the ITAA 1997]***

1.82 Though uncommon, sometimes superannuation is the target of fraudulent or dishonest activities that can result in losses suffered by the superannuation provider. If this loss is brought home to the individual member in respect to their retirement phase interests, and another person is convicted of fraud or dishonesty, the member is entitled to a debit equal to their loss.

Example 1.9: Debits for fraud

James is a member of Cyclist Superannuation Fund. James has $2 million in superannuation and, on 1 July 2018, commenced a superannuation income stream with $1.6 million, leaving the remaining $400,000 in accumulation. James' transfer balance account on 1 July 2018 is $1.6 million.

During the 2018-19 financial year, Cyclist Superannuation Fund invested its pension portfolio in a managed fund called Investments Galore based on financial advice given to the fund by Simon.

In the 2019-20 financial year, it becomes apparent that Investments Galore was a front company set up by Simon to siphon investment income offshore. The money Cyclist Superannuation Fund invested in Investments Galore is lost and the superannuation interest that supports James' superannuation income stream is reduced by $400,000.

Though Cyclist Superannuation Fund is unable to recover the money it lost, in 2020-21 Simon is convicted of fraud in relation to Investments Galore.

James notifies the Commissioner that the superannuation interest that supports his superannuation income stream was reduced by $400,000 because of the fraudulent loss that resulted in Simon's conviction. $400,000 is debited against James' transfer balance account to bring

his balance to $1.2 million. James can use the $400,000 he had remaining in accumulation to replenish his retirement phase interests.

Bankruptcy and void transactions

1.83 Where the superannuation interest that supports an individual's superannuation income stream is reduced because of payments required to comply with the *Bankruptcy Act 1966,* the individual is able to notify the Commissioner and receive a debit in their transfer balance account to the value of the reduction. ***[Schedule 1, Part 1, item 3, item 3 in the table in subsection 294-70(1) and subsections 295-75(5) to (7) of the ITAA 1997]***

1.84 Generally superannuation interests cannot form part of a bankrupt estate. However, there are very specific circumstances where some superannuation contributions can form part of the bankrupt estate and made available to the trustee in bankruptcy.

1.85 Generally, this is only where out of character contributions were made to superannuation with the intent to defeat creditors or to stop the amount becoming part of the bankrupt estate. In these circumstances, the contributions may be required to be transferred out of superannuation to the bankrupt estate.

Example 1.10: Debits for void transactions

Tim runs his own business and, because he is getting close to retirement, in the 2018-19 financial year contributes to his superannuation fund the maximum amount of contributions allowed, being $25,000 of concessional contributions and $300,000 of non-concessional contributions (utilising the three-year bring forward). Previously, Tim only made yearly concessional contributions of $5,000 and no non-concessional contributions since starting his own business.

Tim then retires and commences a superannuation income stream of $1 million on 1 July 2019 with 100 per cent of his superannuation interests, meaning his transfer balance account is also $1 million.

Shortly after this, Tim files for bankruptcy and, notwithstanding Tim's claim that the additional funds were for his retirement, it is determined that the sum of $320,000 contributed in the 2018-19 financial year was an out of character contribution made to defeat the creditors of his business. The trustee of Tim's superannuation fund pays to the bankrupt estate $320,000 as required under the *Bankruptcy Act 1966*.

Tim notifies the Commissioner that the superannuation interest that supports his superannuation income stream has been reduced by $320,000 because of the payment to comply with the *Bankruptcy Act 1966*. Tim's transfer balance account is then debited $320,000 reducing his transfer balance account to $680,000.

Family Law payment splits

1.86 There are circumstances where, following a divorce or other relationship breakdown, superannuation interests may be split as part of the division of property. Under Part VIIIB of the *Family Law Act 1975*, this may occur as a result of a court order or the agreement of the parties. Most commonly, one party (the member spouse) will be required to provide a proportion of their superannuation interests to the other party (the non-member spouse).

1.87 Family law payment splits that occur prior to the individual commencing a superannuation income stream will not affect the individual's transfer balance account as the division occurred prior to the interest entering the retirement phase.

1.88 There are two ways in which a family law payment may affect the superannuation income stream of an individual. Depending on the way the split is given effect to, the appropriate outcome is provided for under either the general debit rules or specific replenishment debit rules.

Application of general rules

1.89 Generally, the member spouse will partially commute their superannuation income stream, receive a superannuation lump sum and pay this amount to the non-member spouse. In these circumstances, a debit will arise in the individual's transfer balance because of the commutation. A replenishment debit does not need to arise in these circumstances. ***[Schedule 1 Part 1, item 3, item 1 in the table in subsection 294-70(1) of the ITAA 1997]***

1.90 If the non-member spouse uses the proceeds of the member spouse's superannuation lump sum to start a new superannuation income stream, the new income stream will give rise to a credit in their transfer balance account. Again, this arises under the general rules outlined above.

Example 1.11: Application of general rules to a payment split

On 1 October 2017 Nancy commenced a superannuation income stream with the value of $1 million. This means Nancy's transfer balance account is credited $1 million.

On 30 September 2018, as part of finalising her divorce, Nancy needs to transfer $500,000 of her superannuation to her ex-partner Michael. Nancy partially commutes her superannuation income stream by the $500,000 and transfers it to Michael's superannuation fund.

Nancy's transfer balance account is debited by $500,000 meaning her transfer balance is now $500,000.

Michael uses $200,000 of the amount he receives to start his own superannuation income stream. He receives a $200,000 credit in his transfer balance account.

Application of replenishment debit rules

1.91 In some uncommon cases, the family law payment split may have the effect of splitting the superannuation income stream benefits attached to the member spouse's superannuation income stream. That is, the member spouse will retain complete ownership of the superannuation interest but a portion of each superannuation income stream benefit (or payment) they receive will be directed to the non-member spouse.

1.92 The member spouse is entitled to a debit in their transfer balance account equal to the value of the superannuation interest that the non-member spouse is effectively entitled to. ***[Schedule 1, Part 1, item 3, item 4 in the table in subsection 294-70(1), subsection 295-80(2) and paragraph 294-80(3)(a) of the ITAA 1997]***

1.93 The non-member spouse receives a credit in their transfer balance account equal to the full value of member spouse's superannuation interests they are partially entitled to. To address the overvaluation of the non-member spouse's credit, they also receive a debit to reflect the member spouse's retained entitlement. ***[Schedule 1, Part 1, item 3, paragraph 294-80(3)(b) of the ITAA 1997]***

1.94 Each spouse must notify the Commissioner in order for their respective debit to arise. The debit arises at the time the payment split becomes operative under the *Family Law Act 1975* or when the individual starts to have a transfer balance account, whichever is later. ***[Schedule 1, Part 1, item 3, subsections 295-80(1) and (4) of the ITAA 1997]***

Example 1.12: Application of the payment split debit rules

Bradley is a member of Guild Workers Superannuation Fund and upon his retirement on 2 February 2015 he starts to receive a pension of $1.6 million. This is the only superannuation interest that Bradley has.

On 1 July 2017 Bradley's transfer balance account is $1.6 million. Bradley's wife, Angie, has not retired and does not have a transfer balance account.

In 2020, Bradley and Angie get divorced and Bradley is required by the family law court orders to split 50 per cent of his superannuation with Angie. However, the rules of Bradley's pension are that it is not capable of being commuted until 10 years after it first commenced. Therefore, it is determined that the family law payment split should apply to the monthly pension payments with Bradley receiving approximately $4,000 and Angie receiving approximately $4,000 per month, commencing 1 October 2020.

Bradley notifies the Commissioner that 50 per cent of the pension payments he receives from his lifetime pension are being paid to Angie as a result of the family law payment split.

Bradley's transfer balance account is debited by $800,000 being the proportion of all the pension payments to be paid to Angie. This means Bradley's transfer balance account is $800,000.

As Angie has started to receive a superannuation income stream, she begins to have a transfer balance account on 1 October 2020. Her account is immediately credited with $1.6 million. This reflects the overall value of the superannuation interest supporting the superannuation income stream to which Angie is now partially entitled.

To correct the inappropriate credit Angie has received, a replenishment debit is also applied, on notification, to Angie's transfer balance account. The debit is $800,000 being Bradley's remaining portion of the pension. Angie's transfer balance is now $800,000.

In both cases, the debit of $800,000 for Bradley and Angie are applied to their transfer balance account with effect from 1 October 2020. Both have a transfer balance account at $800,000. This reflects their effective interest in the pension.

Consequences for future debits

1.95 Generally, family law payment splits that apply to a portion of each superannuation income stream benefit are done this way because the superannuation income stream of the member spouse is not capable of being commuted.

1.96 Where these circumstances change and the superannuation income stream of the member spouse is later commuted, both the member spouse and non-member spouse will receive a superannuation lump sum because a superannuation income stream of which they were the retirement phase recipients is commuted. Consequently, both the member spouse and the non-member spouse will receive a debit for the value of the superannuation lump sum they receive in their transfer balance account. ***[Schedule 1, Part 1, item 3, item 1 in the table in subsection 294-70(1) of the ITAA 1997]***

1.97 Where a different type of debit arises, because of fraud, bankruptcy or because the superannuation income stream ceases to be in the retirement phase for failing to comply with a commutation authority, the law operates to modify that debit to take into consideration the debit that has already applied in respect of the family law payment split. ***[Schedule 1, Part 1, item 3, subsection 294-80(5) of the ITAA 1997]***

Example 1.13: Future consequences of a payment split

Further to Example 1.12, under the rules of Bradley's pension it is allowed to be commuted 10 years after its commencement.

On 2 February 2025 Bradley decides to commute his pension in full and 50 per cent of the superannuation lump sum (now worth $1.2 million) resulting from the commutation is paid to Angie under the terms of the family law payment split.

A debit of $600,000 arises in Bradley's transfer balance account because of the superannuation lump sum he receives from the commutation. A debit of $600,000 also arises in Angie's transfer balance account for the superannuation lump sum she receives from the commutation. As a result both Bradley and Angie have transfer balances of $200,000 ($800,000 - $600,000).

Both may recommence a pension worth up to $1.4 million.

Debits following a determination

1.98 Two additional types of debits may arise during the process of the Commissioner acting to reduce an individual's excess transfer balance.

1.99 Firstly, where a superannuation income stream provider does not comply with a commutation authority, the provider may lose the earnings tax exemption associated with the relevant superannuation income stream (see paragraphs 1.141 to 1.147). A debit equal to the value of the superannuation income stream arises to reflect that the income stream is no longer in the retirement phase. ***[Schedule 1, Part 1, item 3, item 5 in the table in subsections 294-70(1) of the ITAA 1997]***

1.100 Secondly, there may be circumstances where an individual has insufficient superannuation interests available or commutation to rectify an excess transfer balance. In these circumstances, a debit arises to write-off the excess transfer balance (see paragraphs 1.139 and 1.140). ***[Schedule 1, Part 1, item 3, item 6 in the table in subsections 294-70(1) of the ITAA 1997]***

Excess transfer balance determinations

1.101 The Commissioner may make an excess transfer balance determination (a determination) where an individual has an excess transfer balance in their transfer balance account and is in breach of their transfer balance cap. ***[Schedule 1, Part 1, item 14, section 136-10 in Schedule 1 to the Taxation Administration Act 1953(TAA 1953)]***

1.102 The purpose of the determination is to advise the individual of their excess transfer balance and to crystallise the amount of the

individual's excess. The individual's excess transfer balance is crystallised because further notional earnings that accrue are no longer credited towards the individual's transfer balance account. This is the first step in the process of removing capital the individual has in the retirement phase to bring their transfer balance account in line with their transfer balance cap. ***[Schedule 1, Part 1, item 14, sections 136-1 and 136-5 in Schedule 1 to the TAA 1953]***

1.103 Where the individual has already taken steps to rectify their breach and has removed their excess transfer balance, it is not necessary for the Commissioner to issue a determination. Though the individual may not receive an excess transfer balance determination, they are still liable for excess transfer balance tax (see paragraphs 1.148 to 1.156).

1.104 If the Commissioner issues a determination, it will state the amount of the individual's excess transfer balance as at the date the determination is issued. The amount that must be removed is called the 'crystallised reduction amount' and is the sum of transfer balance credits relating to superannuation income streams in the retirement phase and notional earnings that remain in excess of the individuals transfer balance cap at the date of the determination. ***[Schedule 1, Part 1, item 14, subsection 136-10(3) in Schedule 1 to the TAA 1953]***

1.105 The crystallised reduction amount is the value by which the individual's superannuation income streams must be commuted to bring their transfer balance account back in line with their transfer balance cap.

1.106 The Commissioner may amend or revoke a determination at any time to take into account additional information that comes to his or her attention. ***[Schedule 1, Part 1, item 14, subsection 136-10(4) in Schedule 1 to the TAA 1953]***

1.107 A notice is included with the determination and the notice outlines the default commutation authority that the Commissioner intends to issue if the individual does not make an election to commute a different superannuation income stream. ***[Schedule 1, Part 1, item 14, subsection 136-10(6) in Schedule 1 to the TAA 1953]***

1.108 This default commutation notice sets out the superannuation income stream provider and superannuation income stream from which it is intended the crystallised reduction amount will be commuted. Where there is more than one superannuation income stream provider or more than one superannuation income stream, the notice will state the amount by which each superannuation income stream is intended to be commuted, the sum of which cannot be more than the crystallised reduction amount.

Example 1.14: Excess transfer balance determinations and default commutation notices

On 1 July 2017, Rebecca commences a superannuation income stream of $1 million from the superannuation fund her employer contributed to (Master Superannuation Fund). On 1 October 2017, Rebecca also commences a $1 million superannuation income stream in her SMSF, Bec's Super Fund.

On 1 July 2017, Rebecca's transfer balance account is $1 million. On 1 October 2017, Rebecca's transfer balance is credited with a further $1 million bringing her transfer balance account to $2 million. This means that Rebecca has an excess transfer balance of $400,000.

On 15 October 2017, the Commissioner issues an excess transfer balance determination to Rebecca setting out a crystallised reduction amount of $401,414 (excess of $400,000 plus 14 days of notional earnings). Included with the determination is a default commutation authority which lets Rebecca know that if she does not make an election within 60 days of the determination date the Commissioner will issue a commutation authority to Bec's Super Fund requiring the trustee to commute her $1 million superannuation income stream by $401,414.

Elections

1.109 Where an individual has more than one superannuation income stream, they may elect the income stream or streams that are commuted or partially commuted. The total amount of the commutations specified in the individual's election must equal the crystallised reduction amount. ***[Schedule 1, Part 1, item 14, section 136-20 in Schedule 1 to the TAA 1953]***

1.110 The individual must make the election on the approved form to the Commissioner within 60 days from when the date the determination was issued (or such further time as the Commissioner allows). ***[Schedule 1, Part 1, item 14, subsection 136-20(4) in Schedule 1 to the TAA 1953]***

1.111 The individual's election is irrevocable and the Commissioner will issue commutation authorities in accordance with the election. ***[Schedule 1, Part 1, item 14, subsection 136-20(5) in Schedule 1 to the TAA 1953]***

1.112 If the superannuation income stream the individual wishes to have commuted is the same superannuation income stream included in the default commutation notice issued by the Commissioner, it is not necessary for the individual to make an election.

Notifying the Commissioner of transfer balance debits

1.113 After receiving a determination, an individual may advise the Commissioner, in the approved form, of a debit that has arisen in their transfer balance account. A debit may arise where a superannuation income stream of the individual has been fully or partially commuted after the determination was issued. Advising the Commissioner of these amounts allows the Commissioner to determine whether the individual still has an excess transfer balance and whether there is a requirement to issue a commutation authority. ***[Schedule 1, Part 1, item 14, section 136-25 in Schedule 1 to the TAA 1953]***

1.114 The individual must notify the Commissioner in the approved form before the individual makes an election and before the end of the 60-day period in which they are allowed to make the election.

Example 1.15: Transfer balance debits notified after a determination

Further to Example 1.14, Rebecca became aware that she had breached her transfer balance cap on 12 October 2017 and put in place instructions with the accountant that manages Bec's Super Fund to partially commute her superannuation income stream by $500,000.

On 20 October 2017, the superannuation income stream provided by Bec's Super Fund is partially commuted, with $500,000 being placed in an accumulation interest within the fund.

As the debit from the partial commutation arises after the Commissioner issued the determination, Rebecca notifies the Commissioner in the approved form that a debit of $500,000 arose in her transfer balance account on 20 October 2017.

Rebecca's transfer balance account on 15 October 2017 was $2,001,414 ($2 million plus 14 days of notional earnings on an excess of $400,000). After the applying the debit of $500,000, Rebecca transfer balance account is $1,501,414 on 20 October 2017.

As Rebecca no longer has an excess transfer balance in her transfer balance account the Commissioner revokes the determination that was issued to her. This means the Commissioner is not required to issue a commutation authority.

Objections

1.115 Where an individual is dissatisfied with an excess transfer balance determination that has been issued to them, they may object against the determination under the standard objection regime for taxation matters, Part IVC of the TAA 1953. An individual may wish to lodge an objection if the Commissioner did not know about, or did not take into

account, certain debits that arose before the Commissioner issued the determination or otherwise made an error in making the determination. ***[Schedule 1, Part 1, item 14, subsection 136-15(1) in Schedule 1 to the TAA 1953]***

1.116 The individual has 60 days from the date the determination was served on them to lodge an objection against the determination (see paragraph 14ZW(1)(c) of the TAA 1953*)*.

1.117 The default commutation notice included with the determination does not form part of the taxation decision to which the individual can object. ***[Schedule 1, Part 1, item 14, subsection 136-15(2) in Schedule 1 to the TAA 1953]***

1.118 This is because the default commutation notice is only intended to notify the individual of the superannuation income stream(s) in respect of which the Commissioner intends to issue a commutation authority if the individual does not make an election. The individual can choose a different superannuation income stream to be commuted by making an election as discussed in paragraphs 1.109 to 1.112.

1.119 An excess transfer balance determination is included in section 14ZVA of the TAA to limit objection rights against later excess transfer balance tax assessments to grounds that neither were – nor could have been – grounds for objection against the determination. This prevents the Commissioner from having to apply resources to addressing the same objection grounds twice. ***[Schedule 1, Part 1, item 11, paragraph 14ZVA(c) of the TAA 1953]***

Commutation authorities

Issuing of commutation authorities

1.120 The Commissioner is required to issue a commutation authority if a determination has been issued to an individual and – if the individual has notified the Commissioner about any subsequent debits – the debits fall short of the crystallised reduction amount stated on the determination. ***[Schedule 1, Part 1, item 14, subsection 136-55(1) in Schedule 1 to the TAA 1953]***

1.121 If the individual has made a valid election for a different superannuation income stream to be commuted then the commutation authority issued by the Commissioner must be in accordance with the individual's election. ***[Schedule 1, Part 1, item 14, paragraph 136-55(2)(b) in Schedule 1 to the TAA 1953]***

1.122 Where the individual has not made an election to commute a different superannuation income stream the Commissioner will issue a commutation authority consistent with the default commutation notice. ***[Schedule 1, Part 1, item 14, paragraph 136-55(2)(a) in Schedule 1 to the TAA 1953]***

1.123 Where the Commissioner is required to issue a commutation authority but has been notified of debits (as discussed in paragraphs 1.113 and 1.114), the Commissioner may vary the commutation authority from the default commutation notice in a manner that is fair and reasonable so as to take into account the debit. ***[Schedule 1, Part 1, item 14, subsection 136-55(3) in Schedule 1 to the TAA 1953]***

1.124 Each commutation authority issued by the Commissioner must contain:

- the superannuation income stream that the superannuation income stream provider is required to fully or partially commute;
- the amount by which the superannuation income stream is to be commuted (the reduction amount);
- the date issued; and
- any other relevant information.

[Schedule 1, Part 1, item 14, subsection 136-55(4) in Schedule 1 to the TAA 1953]

1.125 The Commissioner may vary or revoke a commutation authority at any time before the Commissioner receives a response from the superannuation income stream provider. ***[Schedule 1, Part 1, item 14, section 136-60]***

1.126 The Commissioner may also issue further commutation authorities where the initial authority is insufficient to achieve the required reduction or, where permitted, the superannuation income stream provider chooses not to comply. ***[Schedule 1, Part 1, item 14, subsection 136-65(1) in Schedule 1 to the TAA 1953]***

Complying with commutation authorities

1.127 A superannuation income stream provider is required to comply with commutation authorities issued to it by commuting the identified income stream by the reduction amount stated in the commutation authority. ***[Schedule 1, Part 1, item 14, section 136-80 in Schedule 1 to the TAA 1953]***

1.128 Where the maximum available release amount of the identified superannuation income stream is less than the reduction amount stated in the commutation authority the superannuation income stream provider is required to commute the superannuation income stream in full.

1.129 The maximum available release amount is defined in section 96-30 in Schedule 1 to the TAA 1953 and means the total amount

of all superannuation lump sums that could be paid from the superannuation interest at that time.

1.130 The superannuation income stream provider is required to reduce the superannuation income stream within 30 days of when the commutation authority is issued.

1.131 A superannuation income stream provider should make reasonable efforts to consult with the individual on whether they wish the amount by which the superannuation income stream is fully or partially commuted to remain within superannuation or, where the individual meets a relevant condition of release, whether they wish it to be paid to them as a superannuation lump sum.

1.132 Where the amount remains in superannuation, the amount will no longer be in the retirement phase and the superannuation income stream provider may need to create an accumulation interest for the individual, if one does not already exist. In determining how to deal with an amount that remains in superannuation, the superannuation income stream provider should consult with the individual member and where this is not possible continue to act in the interests of the member. This may require the superannuation income stream provider to set up an accumulation interest without the consent of the member.

1.133 Where a superannuation income stream provider transfers an amount into an accumulation interest to comply with a commutation authority, the superannuation income stream provider will be subject to the requirement to disclose significant events in section 1017B of the *Corporations Act 2001*. This requirement will assist an individual who has not consented to a transfer to locate the amount.

1.134 Where the amount is paid out of superannuation, the amount will be a lump sum superannuation benefit. For the majority of individuals 60 years of age or over the superannuation lump sum will be tax free. In certain circumstances, the superannuation lump sum will be included in the individual's assessable income and taxed at the individual's marginal income tax rate with a tax offset applying where relevant (see Division 301 of the ITAA 1997).

1.135 The Government will amend the *Corporations Regulations 2001* to allow a superannuation income stream provider to transfer an interest without an eligible application to the superannuation income stream provider. The Government will undertake additional consultation on these amendments at a later date.

Example 1.16: Complying with commutation authorities

Milla has superannuation interests with two superannuation funds, Major Superannuation Fund ($1 million) and Investments Super ($2 million). Before going on an overseas trip, Milla sent instructions to her superannuation funds to commence superannuation income streams as follow:

- $1 million in Major Superannuation Fund, and
- $600,000 in Investments Super.

However, due to a miscommunication, both superannuation funds start superannuation income streams of $1 million on 20 March 2018, meaning Milla exceeded her transfer balance cap by $400,000 on this date.

On 30 March 2018, the Commissioner issues a determination to Milla stating that she has a crystallised reduction amount of $401,009 ($400,000 excess plus 10 days of notional earnings). The determination includes a default commutation authority notice that provides that unless Milla elects otherwise, the Commissioner will issue a commutation authority to Major Superannuation Fund in the amount of $401,009.

Milla has already left for overseas and therefore is not aware of the determination.

On 29 May 2018, the Commissioner issues a commutation authority to Major Superannuation Fund. Major Superannuation Fund tries to contact Milla to find out what she wants, however, as Milla is still overseas, she is still uncontactable.

Major Superannuation Fund considers that, in the absence of Milla's direction, it is in her best interest that the amount remains in superannuation. Major Superannuation Fund partially commutes Milla's superannuation income stream by $401,009 and transfers this amount to an accumulation interest for Milla. Major Superannuation Fund then issues Milla with a new product disclosure statement for her new account.

1.136 A superannuation income stream provider is not required to comply with a commutation authority issued to it if the identified superannuation income stream is a capped defined benefit income stream (see paragraphs 1.157 to 1.167). ***[Schedule 1, Part 1, item 14, subsection 136-80(2) in Schedule 1 to the TAA 1953]***

1.137 Where a superannuation income stream provider is issued a commutation authority, they are required to notify the Commissioner and the individual in the approved form:

- the amount by which the superannuation income stream has been commuted; or
- that the superannuation income stream provider has not complied with the commutation authority because the superannuation income stream is a capped defined benefit income stream.

[Schedule 1, Part 1, item 14, sections 136-85 and 136-90 in Schedule 1 to the TAA 1953]

1.138 The notices must be given within 30 days after the commutation authority was issued. ***[Schedule 1, Part 1, item 14, subsections 136-85(3) and 136-90(2) in Schedule 1 to the TAA 1953]***

Non-commutable excess transfer balance amounts

1.139 In certain circumstances, the Commissioner is required to notify an individual that they have a non-commutable excess transfer balance. This situation may arise where the individual has an excess transfer balance and has no remaining account-based superannuation income streams to be commuted. ***[Schedule 1, Part 1, item 14, section 136-70 in Schedule 1 to the TAA 1953]***

1.140 Where the Commissioner issues a notice in this situation, a debit for the remaining excess balance identified in the notice is applied to the individual's transfer balance account. This is to recognise that although the individual still has an excess transfer balance their only remaining superannuation interests are non-commutable. This effectively writes off the remainder of the excess so that notional earnings do not continue to accrue. ***[Schedule 1, Part 1, item 3, item 6 in the table in subsection 294-70(1) of the ITAA 1997]***

Example 1.17: Non-commutable excess transfer balance.

Marney has superannuation interest with two superannuation funds: $500,000 in her SMSF, MM Super Fund and a defined benefit interest with Government Employees Superannuation Fund.

Marney, who had turned 62 during the year, decides to retire on 1 December 2017 and commences a superannuation income stream in MM Super Fund of $500,000. Her transfer balance account therefore is $500,000 on this date.

The rules of Government Employees Superannuation Fund however, provide that a pension is not payable until Marney turns 65.

On 30 May 2019, when Marney turns 65, she starts to receive a capped defined benefit income stream from Government Employees Superannuation Fund.

The value of Marney's pension from Government Employees Superannuation Fund is $1.6 million (see paragraphs 1.168 to 1.174 for modified valuation rules for capped defined benefit income streams).

On 30 May 2019, Marney's transfer account balance is $2.1 million. Marney's transfer balance cap is $1.6 million (as the general cap has not yet indexed) and Marney has an excess transfer balance of $500,000.

On 9 June 2019, the Commissioner issues a determination to Marney with a crystallised reduction amount of $501,262 and a default commutation notice identifying MM Super Fund. The crystallised reduction amount includes $1,262 of notional earnings that were credited to Marney's transfer balance account between 30 May and 9 June 2019.

On 13 August 2019, the Commissioner issues a commutation authority to MM Super Fund for $501,262 as Marney has not elected a different superannuation income stream to commute.

The balance of Marney's superannuation income stream in MM Super Fund is $380,000 due to superannuation income stream payments and some negative returns over the last five years. On 15 August 2019 MM Super Fund commutes Marney's superannuation income stream in full moving the $380,000 back into an accumulation interest. MM Super fund notifies the Commissioner and Marney of this.

On 15 August 2019, a debit for the full commutation of $380,000 arises in Marney's transfer balance account, reducing her balance to $1,721,262 and her excess to $121,262.

Although Marney still has an excess transfer balance after the debit is applied, the Commissioner is aware that Marney's only other superannuation income stream is a capped defined benefit income stream.

On 20 August 2019, the Commissioner issues a non-commutable excess transfer balance notice to Marney for the amount of $121,262 meaning a debit for that amount arises on that date and Marney's transfer balance account again equals her cap of $1.6 million. Notional earnings cease to arise.

Consequences of not complying with a commutation authority

1.141 Where a commutation authority has been issued in respect of a superannuation income stream and the superannuation income stream provider is required to comply with the authority but has failed to do so, the income stream will not be in the retirement phase. ***[Schedule 8, Part 1, item 14, subsection 307-80(4) of the ITAA 1997]***

1.142 The consequence of the superannuation income stream not being in the retirement phase is that the income stream will no longer qualify for the earnings tax exemption in Subdivision 295-F of the ITAA 1997.

1.143 The superannuation income stream will cease to be in the retirement phase from the start of the financial year in which the superannuation income stream provider failed to comply with the commutation authority and all later financial years. This means that an earnings tax exemption cannot be claimed in respect of the superannuation income stream for that financial year (the year in which the commutation authority was not complied with) or any later financial year.

1.144 A debit arises in the individual's transfer balance account for the value of the superannuation interest that supports the superannuation income stream that has ceased to be in the retirement phase because the superannuation income stream provider has failed to comply with the commutation authority. The debit arises at the end of the period in which the superannuation income stream provider was required to comply with the commutation authority. Generally, this will mean that the individual no longer has an excess transfer balance at this time. ***[Schedule 1, Part 1, item 3, item 5 of the table in subsection 294-70(1) of the ITAA 1997]***

1.145 If the individual wishes to again have a superannuation income stream in the retirement phase – and have it qualify for the earnings tax exemption – they will need to commute the superannuation income stream in full and start a new superannuation income stream. The individual will not get a debit for this commutation as the superannuation income stream will not be in the retirement phase at this time and a debit has already arisen with respect to the income stream.

Example 1.18: Consequences of non-compliance

On 15 January 2018, Craig commences a $3 million superannuation income stream in his SMSF, Cormac Super Fund. Craig's transfer balance account is $3 million and he has a $1.4 million excess transfer balance on this date.

On 20 January, the Commissioner issues a determination to Craig stating his crystallised reduction amount as $1,401,765 ($1.4 million excess plus 5 days of notional earnings). Craig does not have any other superannuation income streams and therefore Craig does not make an election.

On 13 April 2018, the Commissioner issues a commutation authority to Cormac Super Fund requiring the trustee to partially commute Craig's $3 million superannuation income stream by $1,401,765.

Craig does not think he should have to commute his superannuation income stream and therefore, as trustee of Cormac Super Fund, chooses not to comply with the commutation authority.

On 14 May 2018, as Cormac Super Fund has failed to comply with the commutation authority, Craig's $3 million superannuation income stream ceases to be in the retirement phase with effect from 1 July 2017. Consequently, Cormac Super Fund is not eligible to claim any earnings tax exemption in respect of this superannuation income stream for the 2017-18 income year or a later income year.

When Craig's superannuation income stream ceased to be in the retirement phase, a debit arises in Craig's transfer balance cap for the value of the superannuation interest that supported the superannuation income stream. In this case, the debit is $3 million.

Therefore, Craig's transfer balance account on 14 May 2018 is $1,765 ($3,001,765 less $3,000,000). Craig is entitled to commute his superannuation income stream and start a new superannuation income stream in the retirement phase with up to $1,598,235.

1.146 A superannuation income stream provider does not fail to comply with a commutation authority if:

- it commuted the superannuation income stream by the maximum available release amount, or
- it was not required to comply with the commutation authority because the identified superannuation income stream was a capped defined benefit income stream.

1.147 The requirement to comply with a commutation authority is also a regulatory provision for SMSFs. ***[Schedule 1, Part 1, item 9, subparagraph 38A(ab)(iii) of the Superannuation Industry (Supervision) Act 1993]***

Excess transfer balance tax

1.148 Excess transfer balance tax is applied to an individual's accrued amount of notional earnings over a financial year (annualised notional earnings). The annualised notional earnings may relate to multiple periods when the individual had an excess transfer balance. Moreover, notional earnings are taxable regardless of whether the individual has rectified their breach and removed the notional earnings amount from the retirement phase. ***[Schedule 1, Part 1, item 3, section 294-215 of the ITAA 1997; and the exposure draft of the Superannuation (Excess Transfer Balance) Imposition Bill 2016, sections 3 to 5]***

1.149 The standard rate of excess transfer balance tax is 15 per cent. Although based on a notional earnings rate rather than actual earnings,

this tax is intended to neutralise the advantage the individual receives from the superannuation provider's earnings tax exemption. This reflects that, but for the individual's breach, the excess amount on which notional earnings are calculated would have been in the accumulation-phase and taxed at 15 per cent. ***[Schedule 1, Part 1, item 3, section 294-210; and the exposure draft of the Superannuation (Excess Transfer Balance) Imposition Bill 2016, paragraph 5(a)]***

1.150 Notional earnings generally compound daily while the individual has an excess transfer balance. However, once the Commissioner issues a determination to the individual, notional earnings are no longer credited to the individual's transfer balance account. This means that, between the time of the determination and the time the excess transfer balance is commuted, notional earnings continue to arise but they do not compound.

Example 1.19: Excess transfer balance tax

Further to Example 1.6, Andrew starts a second pension worth $1 million. Andrew had no available cap space, meaning he has breached his cap for a second time and has an excess transfer balance of $1 million.

60 days later, the Commissioner issues a determination to Andrew identifying a crystallised reduction amount of $1,015,236 ($1 million excess plus 60 days of notional earnings).

65 days after issuing the determination, the Commissioner issues a commutation authority to Andrew's superannuation fund.

10 days after the Commissioner issues the commutation authority, Andrew's superannuation fund complies with the authority and makes a partial commutation of Andrew's pension, paying Andrew a lump sum of $1,015,236.

Notional earnings accrue to Andrew during the 60-day period before the determination and the subsequent 75-day period before the fund partially commuted the pension.

The Commissioner assesses Andrew for excess transfer balance tax as follows:

Excess	***Period***	***Notional Earnings***
$400,000	30 days (see Example 1.6)	$3,036
$1,000,000	60 days	$13,759
$1,015,236	75 days	$19,192
	TOTAL:	**$37,464**
	Tax (at 15 per cent):	**$5,620**

Note that the notional earnings that accrue during the 75-day period are calculated according to simple interest. This reflects that notional earnings are not credited to Andrew's transfer balance account once the Commissioner issues the determination. The other notional earnings amounts compound daily.

1.151 A tax rate of 30 per cent applies to additional excess transfer balance tax assessments the individual receives in a subsequent financial year. An individual who breaches their transfer balance cap after receiving an assessment in an earlier financial year most likely believes their actual earnings will exceed the notional earnings rate. Imposing a higher rate of taxation is designed to discourage such behaviour. That is, the higher rate includes a deterrent effect in addition to a restorative effect. ***[The exposure draft of the Superannuation (Excess Transfer Balance) Imposition Bill 2016, paragraph 5(b)]***

Example 1.20: Subsequent excess transfer balance tax assessments

Further to Example 1.19, in the following financial year, Andrew starts an additional pension that breaches his transfer balance cap. Andrew rectifies the breach before the Commissioner becomes aware of the subsequent breach.

The Commissioner subsequently identifies the breach and issues an excess transfer balance tax assessment for the financial year. The Commissioner calculates the amount of notional earnings and assesses tax on Andrew at the rate of 30 per cent.

1.152 It is inappropriate for an individual to breach their transfer balance cap. Schemes designed to breach an individual's transfer balance cap for the purpose of producing a tax benefit are subject to the general anti-avoidance rules in Part IVA of the *Income Tax Assessment Act 1936*. Part IVA may also apply to other schemes that seek to circumvent the

transfer balance cap, for example washing assets through the pension phase.

1.153 An excess transfer balance tax assessment is due and payable 21 days after the Commissioner issues the assessment. ***[Schedule 1, Part 1, item 3, section 294-225 of the ITAA 1997]***

1.154 If the Commissioner issues an amended excess transfer balance tax assessment, the additional amount of assessed excess transfer balance tax is due and payable 21 days after the Commissioner issues the amended assessment. ***[Schedule 1, Part 1, item 3, section 294-230 of the ITAA 1997]***

1.155 Where the amount of excess transfer balance tax is not paid by the required time, the general interest charge will start accruing on the unpaid amount. ***[Schedule 1, Part 1, item 3, section 294-235 of the ITAA 1997]***

1.156 Where an individual is dissatisfied with an excess transfer balance assessment, they may object under Part IVC of the TAA 1953 (see paragraph 1.259 below and section 155-90 in Schedule 1 to the TAA 1953).

Capped defined benefit income stream modifications

1.157 Modifications to the general transfer balance cap apply in relation to certain defined benefit income streams. Defined benefit superannuation income streams differ from more common account-based superannuation interests that reflect member contributions. Many defined benefit superannuation income streams are subject to commutation restrictions, which make the application of the general rules inappropriate.

1.158 The modifications include modified valuation rules for certain defined benefit income streams. A further modification prevents an individual from having an excess transfer balance to the extent the excess is attributable to certain defined benefit income streams. ***[Schedule 1, Part 1, item 3, sections 294-105 and 294-110 of the ITAA 1997]***

1.159 Superannuation income stream benefits to which these modifications apply are subject to additional income tax rules (see paragraphs 1.187 to 1.204).

1.160 The purpose of these modifications is to provide broadly commensurate treatment to certain non-commutable superannuation income streams while recognising that it is inappropriate to require individuals to undertake commutations.

1.161 The scope of the rules is limited to certain defined benefit income streams commenced prior to 1 July 2017 and later defined benefit

income streams that generally relate to an employee's long-standing employment entitlements.

Capped defined benefit income streams

1.162 The modifications outlined above apply to certain non-commutable superannuation income streams referred to as capped defined benefit income streams. The concept of a capped defined benefit income stream does not depend on the concept of a defined benefit interest. Rather, the definition is based on a list of superannuation income stream products that are subject to commutation restrictions under the SISR 1994 or the RSAR 1997.

1.163 There are two categories of superannuation income streams the definition applies to:

- those that are covered regardless of when the superannuation income stream started; and
- those that are only covered if the superannuation income stream existed on 30 June 2017.

Capped defined benefit income streams starting on or after 1 July 2017

1.164 Only lifetime pensions are subject to the modifications on an ongoing basis. Lifetime pensions are often provided as employment benefits to Commonwealth, State and Territory public office holders (for example, judges), and military and civilian employees. The extension of the modifications to these pensions reflects that, while the pension itself may not have started before the application of these amendments, the pension is part of a long-standing arrangement. ***[Schedule 1, Part 1, item 3, paragraph 294-115(1)(a) and item 1 in the table in subsection 294-115(3) of the ITAA 1997]***

1.165 In addition, the modifications will not apply to deferred superannuation income streams. Deferred superannuation income streams are a new product and will not exist on 30 June 2017 (see paragraphs 8.30 to 8.37). They do not reflect any long-standing arrangement to justify the application of the modifications. ***[Schedule 1, Part 1, item 3, paragraph 294-115(1)(b) of the ITAA 1997]***

Capped defined benefit income streams existing on 30 June 2017

1.166 A number of other superannuation income streams are eligible for the capped defined benefit income stream rules because they existed prior to the application of these amendments. This application is limited to superannuation income streams that are subject to commutation

restrictions under the SISR 1994 (or RSAR 1997), which apply to the following:

- lifetime pensions not provided by a superannuation fund;
- lifetime annuities;
- life expectancy pensions and annuities;
- market-linked pensions and annuities.

[Schedule 1, Part 1, item 3, subsection 294-115(2) and items 2 to 7 in the table in subsection 294-115(3) of the ITAA 1997]

1.167 Life expectancy and market-linked products are collectively referred to as term products (or term pensions and term annuities as appropriate).

Valuation of capped defined benefit income streams

1.168 Modifications apply to the valuation of capped defined benefit income streams. The rules allow an individual to determine the special value of a capped defined benefit income stream. This special value amount only applies for the purposes of an individual's transfer balance account. However, the transfer balance account is used to determine an individual's eligibility in relation to other areas of the law, for example, to make catch-up concessional contributions (See Chapter 6). ***[Schedule 1, Part 1, item 3, subsection 294-120(1) of the ITAA 1997]***

1.169 Lifetime pensions and annuities that are capped defined benefit income streams are valued by multiplying the annual entitlement by a factor of 16. The purpose of this rule is to provide a simple valuation rule based on general actuarial considerations. This means that a defined benefit pension that pays $100,000 per annum would fully exhaust the $1.6 million transfer balance cap in the 2017-18 financial year. ***[Schedule 1, Part 1, item 3, subsection 294-120(2) of the ITAA 1997]***

1.170 Term pensions and term annuities are valued according to the superannuation income stream's annual entitlement multiplied by the number of years (rounded up to the nearest whole number) remaining on the term of the product. ***[Schedule 1, Part 1, item 3, subsection 294-120(3) of the ITAA 1997]***

Annual entitlements

1.171 An individual's annual entitlement to a superannuation income stream means the total amount of superannuation income stream benefits they are entitled to receive during a 12-month period. The 12-month

period is prospective, beginning at the time the modified valuation rules apply to the capped defined benefit income stream. ***[Schedule 1, Part 1, item 3, subsection 294-120(2) of the ITAA 1997]***

Example 1.21: Annual entitlements and valuation

On 30 June 2017, Sarah is the recipient of a lifetime pension. Under the terms of the pension, Sarah is entitled to receive $5,000 on the 1st day of every month. Sarah is entitled to 12 such payments during the next 12 months. Her annual entitlement is $60,000. Applying the multiplication factor of 16, Sarah's pension has a special value of $960,000. A credit arises in Sarah's transfer balance account for this amount.

Example 1.22: Valuation of term products

Grant purchased a market-linked pension in January 2017. The term of the pension is five years. At 30 June 2017, the pension has an annual entitlement of $100,000. The remaining term is rounded up to five years. The pension has a special value of $500,000.

1.172 The Government acknowledges the approach outlined above may be difficult to apply where the superannuation income stream is subject to indexation. The Government has also considered annualising the first payment an individual receives. However, this may cause difficulties where the first payment of a superannuation income stream is abnormal, as is sometimes the case. The Government is continuing to consider alterative definitions to achieve an outcome based on the first regular payment an individual receives and invites comments on how this issue may be addressed.

Credit and debit amounts arising from capped defined benefit income streams

1.173 The modified valuation rules discussed above are used to determine the amount of credits and debits that arise in relation to capped defined benefit income streams.

1.174 When a capped defined benefit income stream causes a credit to arise in an individual's transfer balance account, the amount of the credit is the superannuation income stream's special value (see Example 1.21).

Debit value

1.175 The debit amount that arises in relation to a capped defined benefit income stream is worked out by reference to the superannuation income stream's debit value.

1.176 The debit value of a lifetime pension or annuity is the residual of its special value, taking into account previous associated debit amounts. This ensures that the total debits an individual receives in relation to a lifetime pension or annuity they fully commute will equal the amount of credits associated with the superannuation income stream. ***[Schedule 1, Part 1, item 3, subsection 294-130(3) of the ITAA 1997]***

Example 1.23: Debit value of lifetime pensions and annuities

Mark starts a lifetime pension that has a special value of $1 million. The debit value of the pension at this time is $1 million.

Later, a debit of $300,000 arises in relation to the pension. From this time, the debit value of the pension is $700,000.

1.177 The debit value of a term product is the superannuation income stream's special value at the relevant time. This valuation will incorporate the ordinary decline in value of a term product, regardless of whether associated debits have previously arisen. ***[Schedule 1, Part 1, item 3, subsection 294-130(4) of the ITAA 1997]***

Example 1.24: Debit value of a term product

Further to Example 1.22, Grant's pension has an initial debit value of $500,000.

On 30 June 2018, Grant's pension has an annual entitlement of $90,000. The remaining term of the pension is four years. The pension has a debit value of $360,000.

Table 1.1: Summary of special valuation rules for capped defined benefit income streams

Product	***Product definition***	***Special value***	***Debit value***
Lifetime pensions	SISR 1994 subregulation 1.06(2)	Annual entitlement multiplied by 16	Starting special value less previous debits
Lifetime annuities	SISR 1994 subregulation 1.05(2)		
Life expectancy pensions	SISR 1994 subregulation 1.06(7)	Annual entitlement multiplied by remaining term	Special value at the relevant time
Life expectancy annuities	SISR 1994 subregulation 1.05(9)		
Market-linked pensions	SISR 1994 subregulation 1.06(8); and RSAR 1997 subregulation 1.07(3A)		
Market-linked annuities	SISR 1994 subregulation 1.05(10)		

Additional capped defined benefit income streams

1.178 The *Income Tax Assessment Regulations 1997* may prescribe additional superannuation income streams that are subject to these rules. If the regulations prescribe additional superannuation income streams, they will also prescribe modified valuation rules and debit value rules in relation to the new income streams. ***[Schedule 1, Part 1, item 3, subsections 294-115(4), 294-120(4) and 294-130(5) of the ITAA 1997]***

Debit amounts

1.179 The debit amount that arises for a full commutation of a superannuation income stream equals the superannuation income stream's debit value at that time. ***[Schedule 1, Part 1, item 3, paragraph 294-130(1)(a) of the ITAA 1997]***

Example 1.25: Debit amount for full commutation

Further to Example 1.23, Mark later makes a full commutation of his lifetime pension. A debit of $700,000 arises in Mark's transfer balance account.

Further to Example 1.24, on 30 June 2018, Grant fully commutes his pension. A debit of $360,000 arises in Grant's transfer balance account.

1.180 The debit amount that arises for a partial commutation is a proportion of the superannuation income stream's debit value. The

proportion is worked out by dividing the lump sum the individual receives for the commutation by the actual value of the superannuation income stream at the time. ***[Schedule 1, Part 1, item 3, paragraph 294-130(1)(b) of the ITAA 1997]***

1.181 This debit amount can be expressed in the following formula:

$$debit\ value \times \frac{lump\ sum}{actual\ value} = debit\ amount$$

Example 1.26: Debit amount for partial commutation

In August 2017, Kyle starts a lifetime pension with a special value of $1.6 million. At this time, the debit value of the pension is also $1.6 million.

In September 2017, Kyle makes a partial commutation of 25 per cent of his pension. Kyle received a $500,000 lump sum. Immediately before the commutation, the actual value of the pension was $2 million.

Kyle receives a debit in his transfer balance account for the following amount:

$$\mathbf{\$1.6\ million} \times \frac{\mathbf{\$500{,}000}}{\mathbf{\$2\ million}} = \mathbf{\$400{,}000}$$

The debit value of the pension is reduced by $400,000.

In January 2021, Kyle fully commutes the pension. A debit of $1.2 million arises in his transfer balance account at this time. The total amount of debits Kyle has received ($1.6 million) equal the credits that were applied when the pension commenced.

1.182 The debit amount that arises in relation to a capped defined benefit income stream that is subject to a family law payment split (see paragraphs 1.91 to 1.97) is worked out by applying the superannuation income stream's debit value. ***[Schedule 1, Part 1, item 3, subsection 294-130(2) of the ITAA 1997]***

Example 1.27: Payment split of capped defined benefit income stream

Terri starts to receive a lifetime pension with a special value of $1.6 million on 1 July 2018.

In 2020 Terri and her husband Beu get divorced and Terri is required by the family law court order to split 50 per cent of her superannuation with Beu. However, as Terri's lifetime pension is non-commutable, the 50 per cent family law payment split applies to the monthly pension payments.

Terri notifies the Commissioner that 50 per cent of the pension payments she receives are to be paid to Beu as a result of the family law payment split.

A debit is applied to Terri's transfer balance account for the proportion of pension payments that became payable to Beu, so her transfer balance account is $800,000.

As Beu has commenced to be in receipt of a superannuation income stream his transfer balance account is credited with the special value of $1.6 million and then debited for the proportion of the lifetime pension that remains with Terri meaning his transfer balance account is $800,000.

In 2022 the rules of the superannuation fund that provides Terri's lifetime pension change such that the pension can now be commuted. Terri decides to commute her lifetime pension in full with 50 per cent of the lump sum that arises from the commutation being paid to Beu.

The debit that arises in Terri's transfer balance account is 50 per cent of the debit value being $800,000. Terri's transfer balance account is now nil and she can commence income streams up to her transfer balance cap.

Fifty per cent of the debit value also arises as a debit in Beu's transfer balance cap – he also can now commence new superannuation income streams up to the value of his transfer balance cap.

1.183 It is not necessary to provide rules for other debit events in relation to capped defined benefit income streams. The defined nature of a member's entitlement precludes them from incurring a loss as a result of fraud or voided transactions – any such loss would be incurred by the superannuation provider. Similarly, a capped defined benefit income stream will not cease to be in the retirement phase because of non-compliance with a commutation authority (see paragraph 1.136).

Modification of excess transfer balance

1.184 If an individual has any capped defined benefit income streams, a modification applies when working out whether the individual has an excess transfer balance.

1.185 An individual will not have an excess transfer balance account to the extent their excess would otherwise be attributable to capped defined benefit income streams. This ensures that an individual cannot breach their transfer balance cap if they only have capped defined benefit income streams. ***[Schedule 1, Part 1, item 3, section 294-125 of the ITAA 1997]***

1.186 The extent to which an excess is attributable to capped defined benefit income streams is worked out by reference to an individual's capped defined benefit balance. This balance is a sub-account of the individual's transfer balance account and includes all debits and credits that relate to capped defined benefit income streams. That is, the capped defined benefit balance reflects the net amount of capital an individual has transferred to the retirement phase in respect of capped defined benefit income streams. ***[Schedule 1, Part 1, item 3, subsection 294-125(3) of the ITAA 1997]***

Example 1.28: No excess transfer balance

On 1 August 2017, Jane starts to receive a lifetime pension with a special value of $3 million. $3 million is credited to Jane's transfer balance account and Jane's capped defined benefit balance.

Although Jane's transfer balance account exceeds her $1.6 million transfer balance, Jane does not have an excess transfer balance because the excess is entirely attributable to her capped defined benefit income stream. Notional earnings do not accrue to Jane. Jane is not required to reduce her retirement phase superannuation interests. However, Jane would be subject to additional income tax rules in relation to her defined benefit income (see paragraphs 1.187 to 1.204).

Example 1.29: Reduced excess transfer balance

Further to Example 1.28, on 1 January 2018, Jane purchases a superannuation income stream for $200,000. The superannuation income stream is not a capped defined benefit income stream.

$200,000 is credited to Jane's transfer balance account, which increases to $3.2 million. Jane now has an excess transfer balance of $200,000 being the amount by which her transfer balance account exceeds her capped defined benefit balance.

Jane will be forced to commute the $200,000 superannuation income stream and will be subject to excess transfer balance tax. If the new superannuation income stream is insufficient to fully remove the crystallised reduction amount ($200,000 plus notional earnings), any remaining excess will be written-off (see paragraphs 1.139 and 1.140).

Additional income tax rules for excess defined benefit income

1.187 Excess capped defined benefit income streams do not cause an individual to breach their transfer balance cap. Broadly commensurate treatment is achieved by subjecting these arrangements to additional income tax rules. An individual is liable to additional income tax consequences in respect of capped defined benefit income streams to the extent that that income exceeds a separate defined benefit income cap. ***[Schedule 1, Part 2, item 28, section 302A-1 of the ITAA 1997]***

1.188 Whether the additional income tax consequences will ultimately increase an individual's income tax liability for a financial year will depend on their broader circumstances.

1.189 An individual's defined benefit income is the superannuation income stream benefits they receive from capped defined benefit income streams. ***[Schedule 1, Part 2, item 28, section 302A-15 of the ITAA 1997]***

1.190 Defined benefit income is taxed differently under Divisions 301 and 302 of the ITAA 1997 depending primarily on the age of the beneficiary. Concessional tax treatment is provided for income to which sections 301-10, 301-100, 302-65 or 302-85 of the ITAA 1997 apply.

The defined benefit income cap

1.191 An individual's defined benefit income cap for a financial year is generally equal to the general transfer balance cap for the corresponding financial year divided by 16. ***[Schedule 1, Part 2, item 28, subsection 302A-20(1) of the ITAA 1997]***

Example 1.30: The defined benefit income stream cap

For the 2017-18 financial year, the defined benefit income cap is generally $100,000 (the $1.6 million general transfer balance cap divided by 16).

1.192 An individual's transfer balance account is not relevant to working out the defined benefit income cap or the amount (if any) of the individual's additional income tax liability.

1.193 An individual's defined benefit income cap is reduced if they:

- first become entitled to concessional tax treatment in respect of defined benefit income during a financial year; or
- they are also entitled to other defined benefit income that is not subject to the concessional tax treatment.

1.194 Only defined benefit income that is subject to concessional tax treatment can count towards the cap. If the individual first becomes entitled to that treatment during a financial year, their defined benefit income cap is reduced proportionately. ***[Schedule 1, Part 2, item 28, subsection 302A-20(3) of the ITAA 1997]***

1.195 The reduction is achieved by multiplying the defined benefit income cap by the following amount:

$$\frac{1 + \text{days remaining in the financial year}}{\text{days in financial year}}$$

Example 1.31: Part-year defined benefit income cap

Chris receives defined benefit income in the form of superannuation income stream member benefits from a taxed source. Chris' 60th birthday is 12 September 2017 (one-fifth of the way through the year). Chris becomes entitled to concessional tax treatment on this date.

Chris' defined benefit income cap for the 2017-18 financial year is worked out as follows:

$$\frac{\$1.6 \text{ million}}{16} \times \frac{1 + 291}{365} = \$80{,}000$$

1.196 A separate reduction applies if an individual receives defined benefit income that is not subject to concessional tax treatment under sections 301-10, 301-100, 302-65 or 302-85 of the ITAA 1997. Such non-concessional defined benefit income is used to reduce the cap but cannot contribute towards an individual's excess amount. The existing tax treatment for these types of income continues to apply. ***[Schedule 1, Part 2, item 28, subsections 302A-20(2) and (4) of the ITAA 1997]***

Example 1.32: Cap reduction for non-concessional income

Brian, aged 57, receives $75,000 of superannuation income stream member benefits and $15,000 of dependant death benefits each year. Brian receives the death benefits because of an entitlement to the superannuation interests of his late wife, Samantha, who was 61 when she died.

Brian is entitled to treat death benefits as non-assessable non-exempt income under section 302-65 of the ITAA 1997but not his member benefits (see section 301-25 of the ITAA 1997).

Brian's defined benefit income cap is reduced by $75,000.

1.197 The reduction for non-concessional income is always applied after any proportionate reduction that applies for a part-year period. If both reductions apply, only non-concessional benefits received after the start of the part-year period are included in the second reduction.

Example 1.33: Applying both reductions to the defined benefit income cap

In 2017-18, Freya, aged 57 and retired, receives defined benefit income of $60,000 from her defined benefit fund. As Freya is under 60 years of age, her benefits are assessable income and she is entitled to a 15 per cent tax offset on that income.

On 1 January 2018 Freya becomes the beneficiary of a taxed-source reversionary pension, and receives $40,000 of defined benefit income from this source in 2017-18. As her spouse was over 60 years of age when he died, these superannuation income stream benefits are treated as non-assessable non-exempt income.

As she commenced receiving this pension half way through the year, Freya's defined benefit income cap is reduced to reflect the proportion of the year in which the reversionary pension was received. That is, her cap is reduced to around $50,000 (half of $100,000).

Freya's defined benefit income cap is then further reduced by the amount of her defined benefit income received from 1 January 2018. That is, her cap is reduced to $20,000 ($50,000 less $30,000, assuming her $60,000 of defined benefit income was paid evenly over the year).

Additional income tax consequences

1.198 Superannuation income streams may be from a taxed or untaxed source, or a combination of the two. The additional taxation consequences are different depending on the source of the excess defined benefit income stream amount. Different rules also apply depending on whether the individual is under 60 years of age.

1.199 Taxed source defined benefit income is considered first and is applied to the defined benefit income cap before untaxed source income. Taxed source superannuation income stream benefits paid to people aged 60 or over are generally non-assessable non-exempt income (section 301-10 of the ITAA 1997). Taxed source death benefits paid to a person aged 60 or over, or where the deceased was 60 or over, are also non-assessable non-exempt income (section 302-65 of the ITAA 1997).

1.200 To the extent an individual's taxed sourced or tax-free defined benefit income exceeds their defined benefit income cap, 50 per cent of the amount is included in their assessable income. ***[Schedule 1, Part 2, item 28, section 302A-5 of the ITAA 1997]***

Example 1.34: Consequences for taxed source benefits

In the 2017-18 financial year, Frances, aged 62, receives defined benefit income of $160,000 from her funded defined benefit scheme.

The defined benefit income cap for the 2017-18 financial year is $100,000 (the $1.6 million general transfer balance cap divided by 16).

Frances' defined benefit income exceeds the income cap by $60,000. Therefore, $30,000 (50 per cent of the $60,000 excess) is included in her assessable income.

1.201 Untaxed source income is considered next. Untaxed source superannuation income stream benefits are generally assessable income subject to a 10 per cent tax offset (sections 301-100 and 302-85 of the ITAA 1997). Excess untaxed source defined benefit income, however, is not entitled to the tax offset and is assessable at the individual's full marginal rate.

1.202 Excess untaxed source defined benefit income is worked out by applying the individual's untaxed defined benefit income stream payments to any amount remaining in their defined benefit income cap (after having applied taxed source defined benefit income). Any amount that exceeds the cap is not entitled to the tax offset. ***[Schedule 1, Part 2, item 28, section 302A-10 of the ITAA 1997]***

Example 1.35: Consequences for untaxed source benefits

In 2017-18 Gordon, aged 65, receives defined benefit income of $140,000 from his unfunded defined benefit scheme. His pension income is taxed at marginal rates, subject to a 10 per cent offset.

However, the amount of any tax offsets Gordon is entitled to receive is reduced by an amount equal to 10 per cent of the excess of his untaxed source defined benefit income over the defined benefit income cap. His pension income offset is therefore effectively capped at $10,000.

That is, his offset entitlement of $14,000 (10 per cent of his $140,000 pension income), is reduced by $4,000 (10 per cent of $40,000 – the excess of his pension income over the income cap).

1.203 Some superannuation income streams contain both taxed elements and untaxed elements.

Example 1.36: Hybrid defined benefit pensions

Paul, who is 61, has a hybrid defined benefit pension and receives $180,000 of defined benefit income in 2017-18. Half of the pension is from an untaxed source and the other half is taxed.

The entire $90,000 of taxed income is counted towards Paul's $100,000 defined benefit income cap. $10,000 of the untaxed income is also counted towards the cap, exhausting it. The remaining $80,000 of untaxed income is denied a tax offset under section 301-100 of the

ITAA 1997. Paul's section 301-100 tax offset is limited to $1,000 (10 per cent of the $10,000 counted towards the cap).

The same outcome would occur if the two elements were from separate superannuation income streams, regardless of when either stream was established.

1.204 Further examples of these rules are provided below.

Example 1.37: Death benefits

On 1 October 2017, Naomi, aged 63, becomes the beneficiary of a reversionary pension, and receives $80,000 of defined benefit income from this source in 2017-18.

As she commenced receiving this pension part way through the year, Naomi's defined benefit income cap is reduced to reflect the proportion of the year in which the reversionary pension was received. That is, her cap is reduced to around $75,000 (three quarters of $100,000).

Naomi's defined benefit income from the reversionary pension exceeds her defined benefit income cap by $5,000 ($80,000 less $75,000). Therefore, she will have to include $2,500 (50 per cent of the $5,000 excess) in her assessable income.

Example 1.38: Death benefits and member benefits

Further to Example 1.33, Freya's defined benefit income from her reversionary pension exceeds her defined benefit income cap by $20,000 ($40,000 less $20,000).

Therefore, she will have to include $10,000 (50 per cent of the $20,000 excess) in her assessable income.

Modifications for child dependants

1.205 A child recipient that receives superannuation death benefits from a parent is entitled to a modified transfer balance cap. This ensures that a child does not exhaust their normal transfer balance cap before they reach retirement age. ***[Schedule 1, Part 1, item 3, sections 294-155 and 294-160 of the ITAA 1997]***

1.206 A child recipient is a deceased person's dependant child that is under the age of 25. If the child is between 18 and 25, the child must also be financially dependent on the other person to qualify to receive a superannuation death benefit income stream. A deceased's child is also a dependant if they have a permanent disability, regardless of their age.

(SISR 1994 subregulation 6.21(2A) and RSAR 1997 subregulation 4.24(3A)).

1.207 A child recipient is required to commute all of their superannuation income streams and remove the capital from the superannuation system when they turn 25, unless they have a permanent disability (SISR 1994 subregulation 6.21(2B)). The child's modified transfer balance account will cease either when they commute all their superannuation income streams (consistent with this provision) or the capital is exhausted.

1.208 The exception to this general rule is children with a permanent disability. These children are not subject to the cashing out rule, so their modified transfer balance cap will cease when the funds are exhausted.

The child's transfer balance cap

1.209 The child does not have a personal transfer balance cap set to the value of the general transfer balance cap. Rather, the child's cap is generally determined by reference to the value of the deceased's retirement phase assets that they receive. This is achieved through a series of cap increments that arise in relation to each superannuation income stream the child receives. ***[Schedule 1, Part 1, item 3, section 294-170 of the ITAA 1997]***

1.210 The determination of the child's transfer balance cap will depend on:

- whether the child started to receive superannuation income streams before 1 July 2017;
- if they started to receive them after that time, whether or not the deceased had a transfer balance account at the time of their death; and
- if so, whether the deceased had an excess transfer balance in the retirement phase at the time of their death.

Superannuation income streams received before 1 July 2017

1.211 If a child is receiving superannuation income streams as a child recipient when these amendments begin to apply, the child's transfer balance cap is $1.6 million. This reflects the amount of retirement phase superannuation interests the deceased parent could have had if they had died shortly after 1 July 2017. ***[Schedule 1, Part 1, item 3, section 294-175 of the ITAA 1997]***

Where the deceased parent does not have a transfer balance account

1.212 If the deceased parent did not have a transfer balance account at the time of their death – and they died on or after 1 July 2017 – the child's cap is their proportionate share of the deceased's superannuation interests multiplied by the general transfer balance cap. This situation is most likely to arise where the parent dies before they enter the retirement phase. ***[Schedule 1, Part 1, item 3, section 294-180 of the ITAA 1997]***

Example 1.39: Child's transfer balance cap where deceased parent does not have a transfer balance account – single beneficiary

Craig dies on 15 November 2019 aged 56 with accumulation assets worth $2 million. His 12 year old daughter Eliza is the sole beneficiary of his estate. As Craig has not yet retired, he does not have a transfer balance account. As there are no other beneficiaries, Eliza's share is 100 per cent of the general transfer balance cap. Eliza can take $1.6 million of the $2 million as a superannuation death benefit income stream. The remaining $400,000 would need to be paid to Eliza as a lump sum and removed from the superannuation system.

Example 1.40: Child's transfer balance cap where deceased parent does not have a transfer balance account – multiple beneficiaries

Emma dies on 6 June 2018 aged 55 with accumulation interests worth $2 million. Emma's two daughters Sana and Chloe are the sole beneficiaries of her superannuation interests. Emma has left instructions that her superannuation interests are to be shared equally between Sana and Chloe.

As Emma has not yet retired, her beneficiaries are entitled to their proportion of the general transfer balance cap, expected to be $1.6 million in 2018. Sana and Chloe will each receive a transfer balance cap of $800,000 (50 per cent of the general transfer balance cap). The remaining $200,000 that each child receives would need to be taken as a lump sum and cashed out of the superannuation system.

Where the deceased parent does have a transfer balance account

1.213 If the deceased person did have a transfer balance account, the child beneficiary is entitled to their portion of the deceased's superannuation interests that were in the retirement phase. ***[Schedule 1, Part 1, item 3, subsections 294-185(1) and (2) of the ITAA 1997]***

1.214 If the deceased had a mix of retirement phase and accumulation interests, it is only the retirement phase interests that are included when calculating the child's cap. ***[Schedule 1, Part 1, item 3, subsection 294-185(3) of the ITAA 1997]***

1.215 A cap increment arises with respect to each superannuation income stream the child receives. Each cap increment arises when the child starts to receive the superannuation income stream. However, if the superannuation income stream is a reversionary income stream, the cap increment is deferred for six months to align with the modification discussed at paragraph 1.53. ***[Schedule 1, Part 1, item 3, subsection 294-185(5) of the ITAA 1997]***

Example 1.41: Child's transfer balance cap where deceased parent has a transfer balance account – single beneficiary

Damien dies on 23 March 2018 aged 70 with remaining retirement phase interests worth $1.3 million and accumulation interests of $400,000. Damien's two children, Alyssa, 15, and Zali, 13, are his sole superannuation beneficiaries. Damien leaves advice that his superannuation interests are to be evenly divided between his two children.

Damien's retirement phase interests are divided evenly between his two children. Alyssa and Zali each have a transfer balance cap of $650,000 to cover these interests.

They each receive $200,000 from Damien's accumulation interests but these amounts must be taken out of the superannuation system as superannuation lump sums.

Where the deceased parent has an excess transfer balance

1.216 A child's transfer balance cap is reduced if their deceased parent had an excess transfer balance. The child's cap is reduced by their proportionate share of their parent's excess. However, an amount is not reduced to the extent the child received their superannuation death benefits entitlements as a lump sum. ***[Schedule 1, Part 1, item 3, subsection 294 185(4) of the ITAA 1997]***

Example 1.42: Child dependants

Thomas has a reversionary pension worth $1.7 million. Thomas has a personal transfer balance cap of $1.6 million. His transfer balance account is $1.8 million meaning he has an excess transfer balance of $200,000.

On his death in February 2018, Thomas' pension reverts to his son, Bruce, who is aged 16. Bruce's transfer balance cap is set at $1.5 million (the value of the $1.7 million pension less Thomas's $200,000 excess transfer balance).

Where both parents die

1.217 Where both of a child's parents die, the child's transfer balance cap is the sum of amounts worked out in relation to each parent.

Example 1.43: Child's transfer balance cap where both parents die

Further to Example 1.42, shortly after Thomas' death, Bruce's mother, Martha, also dies. Martha had not retired and did not have a transfer balance account. Martha had accumulation interests worth $4 million of which Bruce is the sole beneficiary.

Bruce receives a cap increment equal to the general transfer balance cap of $1.6 million. Bruce's temporary transfer balance cap is now $3.1 million.

Bruce keeps his father's reversionary pension worth $1.7 million. He can also start a new superannuation income stream worth $1.4 million from his mother's accumulation interests. The remaining $2.6 million must be cashed out of the superannuation system and provided to Bruce as a lump sum.

Ceasing the child's transfer balance account

1.218 The child's transfer balance account ceases when they are forced to commute their superannuation income streams at the age of 25. Alternatively, if all of the child's superannuation income streams cease before that time, their transfer balance account ceases at that time.

1.219 If the child is not required to cash out their superannuation income streams at the age of 25 because they have a permanent disability, their transfer balance account ceases when their superannuation income streams are exhausted or otherwise cease.

1.220 In any case, once a child's transfer balance account ceases, their entire position with respect to the transfer balance account is reset. When they retire many years later, they will likely start a new transfer balance account and have a new transfer balance cap based on the general transfer balance cap. ***[Schedule 1, Part 1, item 3, section 294-165 of the ITAA 1997]***

Example 1.44: Ceasing a child's transfer balance account

Further to Example 1.43, Bruce does not have a disability and must commute his superannuation income streams when he turns 25. At this time, his transfer balance account is reset.

Bruce retires many years later and is subject to the general rules. He commences his own superannuation income stream, starting a new transfer balance account. His new personal transfer balance cap is set

at the amount of the general transfer balance account in that financial year.

CGT relief arrangements

1.221 Part 3 of Schedule 1 to the Bill provides transitional CGT relief arrangements, effectively applying to asset transfers before 1 July 2017. As the relief is a temporary, the provisions will not be inserted into the ITAA 1997. Instead, the provisions will be operative within the amending Act that introduces the transfer balance cap.

1.222 Where individuals need to commute superannuation income streams to transfer amounts from the retirement phase to the accumulation phase to comply with the transfer balance cap, earnings on assets supporting these commuted balances will become taxable. Similarly, where individuals have a TRIS, earnings on assets supporting these superannuation income streams will become taxable from 1 July 2017 as they will no longer be in the retirement phase.

1.223 The object of the provisions is to provide temporary relief for complying superannuation fund from these tax consequences for capital gains accumulated before 1 July 2017, where these gains would have been exempt income if realised prior to the commutation or the change to the treatment of TRIS. ***[Schedule 1, Part 3, item 30]***

1.224 The CGT relief arrangements will allow complying superannuation funds to reset the cost base on CGT assets that are moved or reapportioned from the retirement phase to the accumulation phase prior to 1 July 2017, including assets supporting TRIS.

1.225 These arrangements will replicate the consequences for a fund as if they had triggered a CGT event on these assets prior to 1 July 2017, and ensure that, when these assets are sold after 1 July 2017, tax is only paid on capital gains accrued after this date.

1.226 The CGT relief arrangements are only intended to support movements of assets and balances necessary to support the transfer balance cap and changes to the TRIS. It would be otherwise inappropriate for a fund to wash assets to obtain CGT relief or to use the relief to reduce the income tax payable on existing assets supporting the accumulation phase. Schemes designed to maximise an entity's CGT relief or to minimise the CGT gains of existing assets in accumulation phase may be subject to the general anti-avoidance rules in Part IVA of the *Income Tax Assessment Act 1936*.

1.227 The Government acknowledges that these provisions are complex and include a range of interactions with the CGT and other

income tax provisions of the ITAA 1997. As such, the Government is continuing to consider the best approach to incorporating these provisions in the legislation and welcomes any feedback on the best way to do so.

Segregated current pension assets

1.228 Where a segregated current pension asset within the meaning of subsection 295-385(3) of the ITAA 1997 ceases to be segregated in the period between the date that legislation is introduced and 1 July 2017, a fund may choose to reset the cost base of this asset to its current market value at that time. ***[Schedule 1, Part3, subitem 31(1) and (4) 'pre-commencement period']***

1.229 The choice will need to be made in the approved form before the fund's income tax return for 2016-17 is required to be lodged, and cannot be revoked. ***[Schedule 1, Part 3, subitem 31(2)]***

1.230 The cost base of the asset is reset by assuming the asset had been disposed of, for its market value, at the time the asset ceases to be a segregated current pension asset, and simultaneously reacquired by the fund for that value. ***[Schedule 1, Part 3, subitem 31(3)]***

1.231 As earnings on segregated current pension assets are entirely tax-exempt, there are no further tax consequences for a fund when applying the relief to a segregated asset.

Example 1.45: Applying CGT relief to a segregated asset

Tim (retired) and Laura (still in accumulation) have SMSF which holds a number of assets as segregated current pension assets, to support Tim's $2.6 million superannuation income stream.

To comply with the transfer balance cap, Tim partially commutes $1 million of his superannuation income stream back to the accumulation phase on 30 June 2017. To give effect to this, the fund moves an asset with a market value of $1 million out of the segregated pool of exempt assets.

The cost base for this asset is $750,000, meaning that it already has accrued unrealised capital gains of $250,000. To ensure that these capital gains are not taxed when the asset is eventually sold, the fund chooses to apply the CGT relief arrangements to this asset, resetting its cost base to $1 million.

Asset subject to the proportional method

1.232 Where a fund uses the proportional method provided for in section 295-390 of the ITAA 1997 for an asset in the period between the

date that legislation is introduced and 1 July 2017, and the asset was held by the fund throughout that period, the fund may choose to reset the cost base of this asset to its market value as at 30 June 2017. ***[Schedule 1, Part 3, subitem 32(1) and (5) 'pre-commencement period']***

1.233 The choice will need to be made in the approved form before the fund's income tax return for 2016-17 is required to be lodged. The choice cannot be revoked. ***[Schedule 1, Part 3, subitem 32(2)]***

1.234 The cost base of the asset is reset by assuming the asset had been disposed of, for its market value, immediately before 1 July 2017 and the asset reacquired again by the fund just after the sale for that value. ***[Schedule 1, Part 3, subitem 32(3)]***

1.235 To take advantage of the reset cost base the fund will have to have disposed of the asset within a 10 year window, before 1 July 2027. If it does not do so, it will revert to the asset's original cost base. ***[Schedule 1, Part 3, subitems 32(3) and (4)]***

Treatment of the notional gain attributable to the accumulation phase

1.236 Where a fund chooses to reset the cost base of an asset subject to the proportional method, the fund will also need to calculate the notional gain on this asset as at 30 June 2017 that is attributable to the accumulation phase. This notional gain cannot be negative. ***[Schedule 1, Part 3, subitem 33(1), (4) and (6) 'pre-commencement period' and '2016-17 non-exempt proportion']***

1.237 The fund will need to add this notional gain (if not deferred) to its net capital gain (or loss) for the 2016-17 income year as part of its annual return, in order to crystallise the tax liability that would have arisen if the asset had been sold in that year. ***[Schedule 1, Part 3, subitem 33(1)]***

1.238 Where the notional gain is added to the net capital gain, the notional gain is not subject to the fund's exempt proportion as this proportion has already been captured in the calculation of the notional gain. ***[Schedule 1, Part 3, subitem 33(5)]***

Example 1.46: Applying CGT relief to a proportioned asset

Claire (receives superannuation income stream benefits) and Ashley (still in accumulation) have a SMSF supported by a single asset with a market value of $3 million. The fund uses the proportional method to calculate the proportion of income from the asset that is exempt income, with two-thirds of the asset supporting Claire's $2 million superannuation income stream.

To comply with the transfer balance cap, Claire partially commutes $500,000 of her superannuation income stream back to the

accumulation phase on 30 June 2017. This means the proportion of the fund's assets that support Clair's superannuation income stream is 50 per cent.

The cost base for the asset is $2.5 million, meaning that it already has accrued unrealised capital gains of $500,000. The fund chooses to apply the CGT relief arrangements to this asset, resetting its cost base to $3 million at 30 June 2017.

The fund calculates the notional gain on the asset that is attributable to Ashley's accumulation interest as one-third of $500,000, equal to $166,667. If applicable, the fund also applies the CGT discount to this amount.

The fund must add this amount to its net capital gain (if any) for the 2016-17 year as part of its annual return if it does not choose deferral.

1.239 Where a fund applies the relief to a proportioned asset and calculates a positive notional gain, the fund may choose to defer the inclusion of the notional gain in its annual return until the asset is sold and the gains on the asset are realised. ***[Schedule 1, Part 3, subitem 33(3)]***

1.240 Again, the choice will need to be made in the approved form before the fund's income tax return for 2016-17 is required to be lodged, and cannot be revoked. ***[Schedule 1, Part 3, subitem 33(2)]***

1.241 Where a fund chooses to defer the inclusion of the notional gain, the gain must be added to the fund's net capital gain (or loss) in the income year in which the asset is sold.

1.242 Where the notional gain is added to the net capital gain, the notional gain is not subject to the fund's exempt proportion in that later financial year as the 2016-17 proportion has already been captured in the calculation of the notional gain. ***[Schedule 1, Part 3, subitem 33(5)]***

1.243 Where the fund has not disposed of the asset within a 10 year window, before 1 July 2027, the notional gain ceases to exist as the cost base of the asset will revert to what is was prior to the relief applying. ***[Schedule 1, Part 3, subitem 33(3)]***

Example 1.47: Applying CGT relief to a proportioned asset and deferred inclusion of the notional gain.

Jon (receives superannuation income stream benefits) and Olivia (still in accumulation) have a SMSF supported by a single asset with a market value of $3 million, with two-thirds of the asset supporting Jon's $2 million superannuation income stream.

To comply with the transfer balance cap, Jon partially commutes $500,000 of his superannuation income stream back to the accumulation phase on 30 June 2017. This means the proportion of the fund's assets that support Jon's superannuation income stream is 50 per cent.

The cost base of this asset is $2.5 million, meaning that it already has accrued unrealised capital gains of $500,000. The fund chooses to apply the CGT relief arrangements to this asset, resetting its cost base to $3 million on 30 June 2017.

The fund calculates the notional gain on the asset that is attributable to Ashley's accumulation interest as one-third of $500,000, equal to $166,667. The fund chooses to defer the inclusion of this amount in its annual return until the asset is sold.

In June 2020, the fund sells the asset for $4 million, realising a capital gain of $1 million (from the reset cost base of $3 million). After applying the one-third CGT discount and the exempt proportion of 50 per cent, the fund calculates its net capital gain for the 2019-20 year as $333,333.

The fund adds its deferred notional gain of $166,667 to this net capital gain, bringing its total net capital gains for the 2019-20 income year to $500,000.

If the fund had not sold the asset by 1 July 2027, the deferred notional gain would have ceased to exist as the cost base for the asset would revert to its original level of $2.5 million.

Notional gains not to be included in exempt proportion calculation for relevant year

1.244 Notional gains can either be brought to account in the 2016-17 income year or deferred until the year in which the asset is actually realised. ***[Schedule 1, Part 3, subitems 33(1) and (3)]***

1.245 In either case, the notional gain that is added to the net capital gain under either subitem 33(1) or (3) cannot be included in the exempt proportion calculated under section 295-390 of the ITAA 1997 for the relevant year. ***[Schedule 1, Part 3, subitem 33(5)]***

1.246 This is because the exempt proportion for the 2016-17 income year has already been applied in the calculation of the notional gain in that year.

Consequential amendments

Reporting obligations for life insurance companies

1.247 Life insurance companies will now be required to report to the Commissioner information relating to exempt life insurance policies that provide for annuities in the retirement phase. ***[Schedule 1,Part 1, item 21, section 390-20 in Schedule 1 to the TAA]***

1.248 The reporting requirement is to allow for information about annuities and immediate annuities in the retirement phase to be given to the Commissioner for the purpose of administering the superannuation legislation and in particular the transfer balance cap. The reporting requirement is similar to that which already exists for member information statements for superannuation providers.

1.249 The information must be given in the approved form and the Commissioner may determine by legislative instrument both the period to which the information relates and the date by which the information must be provided.

1.250 Notes are added to provisions in Divisions 301 and 302 of the ITAA 1997 (about the income tax treatment of superannuation income stream member benefits and death benefits) that link to the new rules for excess defined benefit income. ***[Schedule 1, Part 2, items 22 to 27, sections 301-10, 301-90, 301-100, 302-65, 302-80 and 302-85 of the ITAA 1997]***

Income tax withholding and reporting

1.251 A consequential amendment is made to ensure that the Pay-As-You-Go Withholding (PAYG Withholding) regime applies to superannuation income stream benefits that are defined benefit income. The PAYG Withholding regime applies to income stream payments that are not non-assessable non-exempt income (sections 12-1 and 12-80 in Schedule 1 to the TAA 1953). ***[Schedule 1, Part 3, item 29, subsection 12-1(4) in Schedule 1 to the TAA 1953]***

1.252 Superannuation income stream providers may not know whether defined benefit income they pay to members is assessable income because they may not know if the member receives other defined benefit income.

1.253 Ensuring the withholding regime applies provides certainty to providers in relation to both their withholding obligations and associated reporting obligations. Importantly, reporting obligations apply to withholding payments even if the amount required to be withheld is nil.

The reporting obligations, in turn, are important to the effective administration of these amendments.

1.254 The Commissioner will consult separately on the administrative aspects of these amendments, including if any changes are required to withholding schedules.

Other consequential amendments

1.255 The *Administrative Decisions (Judicial Review) Act 1977* is amended to ensure that that Act does not apply to excess transfer balance determinations and other decisions the Commissioner makes in relation to the transfer balance cap. Individuals are instead entitled to object to these decisions under Part IVC of the TAA 1953. ***[Schedule 1, Part 1, item 1, paragraph (gab) in Schedule 1 to the Administrative Decisions (Judicial Review) Act 1977]***

1.256 An individual is not entitled to an income tax deduction for an amount of excess transfer balance tax. ***[Schedule 1, Part 1, item 2, section 26-99 of the ITAA 1997]***

1.257 Consequential amendments are made to Subdivision 960-M of the ITAA 1997 to include references to the new framework for indexing amounts in increments. ***[Schedule 1, Part 1, item 4 to 7, item 10A of the table in section 960-265, Notes 1 and 2 to subsection 960-270(3), Notes 1 and 2 to subsection 960-280(6), and subsection 960-285(1) of the ITAA 1997]***

1.258 Excess transfer balance tax is included in the table of liabilities that attract general interest charge. ***[Schedule 1, Part 1, item 10, item 15B of the table in subsection 8AAB(4) of the TAA 1953***]

1.259 Consequential amendments are made to various provisions in the TAA 1953 to include excess transfer balance within the assessment and tax liability framework. This includes clarifying that excess transfer balance tax cannot be self-assessed. ***[Schedule 1, Part 1, item 15 to 19, paragraph 155-5(2)(h), Note 1 to subsection 155-15(1), subsection 155-30(3), item 38BC in the table in subsection 250-10(2) in Schedule 1 to the TAA]***

1.260 New definitions are inserted into the dictionary definitions of the ITAA 1997. ***[Schedule 1, Part 5, item 36 and 39, subsection 995-1(1) (definitions of 'annualised notional earnings on excess transfer balance', 'assessed excess transfer balance tax', 'capped defined benefit income stream', 'child recipient', 'crystallised reduction amount', 'debit value', 'defined benefit income', 'defined benefit income cap', 'default commutation notice', 'excess transfer balance', 'excess transfer balance determination', 'excess transfer balance tax', 'general transfer balance cap', 'member spouse', 'notional earnings on excess transfer balance', 'notional earnings on excess transfer balance rate', 'retirement phase recipient', 'rounding amount', 'special value', 'superannuation income stream provider', 'transfer balance account', 'transfer balance cap', 'transfer balance credit' and 'transfer balance debit') of the ITAA 1997]***

1.261 Amendments are also made to the definitions of indexation factor and index number. ***[Schedule 1, Part 5, item 37 and 38, subsection 995-1(1) (paragraph (aa) of the definition of 'indexation factor' and paragraph (aa) of the definition of 'index number') of the ITAA 1997]***

Application and transitional provisions

1.262 The amendments commence on the first 1 January, 1 April, 1 July or 1 October to occur after the day the amendments receive Royal Assent. ***[item 2 in the table in section 2 of the exposure draft of the Bill]***

1.263 The transfer balance cap amendments apply on and from 1 July 2017. ***[Schedule 1, Part 3, item 34 and subitem 35(2), section 294-10 of the Income Tax (Transitional Provisions) Act 1997 (IT(TP) 1997)]***

1.264 Similarly, the other matters discussed in this Chapter that apply on a financial year basis – for example the new indexation rules, excess transfer balance determinations, commutation authorities and additional income tax rules for defined benefit income – apply in relation to the 2017-18 financial year and future financial year. ***[Schedule 1, Part 3, subitem 35(1)]***

1.265 New definitions that support the transfer balance cap apply from 1 July 2017. New definitions – and amendments to existing definitions – to support the matters mentioned in 1.264 apply in relation to the 2017-18 and future financial years. ***[Schedule 1, Part 5, item 40]***

1.266 Transitional rules apply to transfer balance cap breaches of less than $100,000 that occur on 30 June 2017. Such breaches do not give rise to notional earnings or an excess transfer balance tax liability if they are rectified within 60 days. ***[Schedule 1, Part 4, item 34, section 294-30 of the IT(TP) Act 1997]***

1.267 The rationale for this relief is that it will be difficult for individuals with existing superannuation income streams to predict their retirement phase balances as at 30 June and ensure they are not in breach of their $1.6 million transfer balance cap. Small breaches of less than $100,000 are likely to be unintentional.

Example 1.48: Transitional rules for small breaches

On 1 January 2017, Ian has an account-based pension worth $2 million. Following the enactment of the transfer balance cap legislation, on 15 June 2017, Ian partially commutes his pension and receives a lump sum of $400,000.

The pension increases in value by $10,000 by 30 June 2017 because of market volatility. The value of the superannuation income stream on 30 June is $1.61 million. A credit arises in Ian's transfer balance account for that amount on 1 July 2017. Ian has an excess transfer balance of $10,000.

On 1 August 2017, Ian makes a partial commutation of the superannuation income stream and receives a debit of $10,000. Because Ian has rectified the breach of his transfer balance cap, and the breach was less than $100,000, no notional earnings accrue to Ian.

1.268 This transitional rule only affects notional earnings. It does not allow an individual that has exceeded their transfer balance cap to gain any benefit from the indexation of the general transfer balance cap.

1.269 Part 3 of Schedule 1 (about CGT relief) applies to CGT assets of complying superannuation funds that either:

- cease to be a segregated current pension asset; or
- are not a segregated current pension asset or segregated non-current asset at any time,

during the period from the date of introduction of the Bill to just before 1 July 2017.

Chapter 2
Concessional superannuation contributions

Outline of chapter

2.1 The exposure draft of Schedule 2 to the Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (the Bill) reduces:

- the annual cap applying to concessional contributions made to superannuation in a financial year to $25,000 (from $30,000 for those aged under 49 at the end of the previous financial year and $35,000 otherwise); and
- the threshold at which high-income earners pay additional tax (Division 293 tax) on their concessionally taxed contributions to superannuation to $250,000 (from $300,000).

2.2 Schedule 2 also amends how concessional contributions are determined to ensure that contributions to constitutionally protected funds and unfunded defined benefit superannuation schemes count towards an individual's concessional contributions cap.

2.3 All references in this Chapter are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise specified.

Context of amendments

2.4 This measure forms part of the Government's Superannuation Reform Package announced in the 2016-17 Budget. It improves the sustainability and equity of the superannuation system.

2.5 The current treatment of concessional superannuation contributions means high-income earners disproportionately benefit from the superannuation tax concessions, in part because they have the capacity to make greater superannuation contributions. As high-income earners will generally save for their retirement, both within and outside the superannuation system, these concessions are poorly targeted.

2.6 Reducing the annual cap on concessional contributions will require high-income individuals to hold a larger portion of their savings outside the concessionally taxed superannuation environment. This reduces their ability to utilise the superannuation system as a tax advantaged savings vehicle.

2.7 Lowering the threshold at which the Division 293 tax applies ensures that the tax concessions provided to those on high incomes (compared to income tax on other income) are more closely aligned with tax concessions provided to middle-income earners.

Reducing the cap on concessional contributions

2.8 Prior to these amendments, the annual cap on concessional contributions to superannuation for a financial year was $30,000 for those aged under 49 at the end of the previous financial year and $35,000 otherwise at the end of the financial year preceding the current year (section 291-20 of the ITAA 1997 and section 291-20 of the *Income Tax (Transitional Provisions) Act 1997* (IT(TP)A 1997)).

2.9 Determining an individual’s concessional contributions cap based on their age effectively amounts to age-based taxation, given that the tax rate on superannuation contributions is typically less than an individual’s marginal tax rate. Removing this bias in favour of Australians aged over 49 in the concessional contributions cap ensures that all individuals of working age have the same concessional contribution cap rules.

2.10 Any increases in the general concessional contributions cap were rounded down to the nearest $5,000 increment, with no increase applying if the increase would be less than $5,000. The $35,000 transitional cap was not subject to indexation, with the intention that eventually it would be overtaken by the general cap and at that time the same cap would apply regardless of age.

Lowering the threshold for Division 293 tax

2.11 In addition, prior to these amendments, if the sum of an individual's:

- income for surcharge purposes less reportable superannuation contributions for an income year (broadly their taxable income disregarding investment losses, plus any reportable fringe benefits); and

- low tax contributions for the corresponding financial year (their concessional contributions less their excess concessional contributions);

exceeded $300,000, the individual was required to pay Division 293 tax.

2.12 This income test provides a broader definition of income than some other income tests but is considered to more accurately reflect whether an individual is a high-income earner.

2.13 Division 293 tax was payable by the individual at a rate of 15 per cent on the lesser of:

- the amount by which that sum exceeded $300,000; or
- the individual's low tax contributions (see section 293-25).

2.14 This means Division 293 tax applies to the whole amount of an individual’s concessional contributions (excluding excess concessional contributions) if an individual’s income (as modified above) exceeds $300,000. Otherwise the additional tax is only imposed on the portion of the contributions that takes the sum of the individual’s relevant contributions and income over $300,000.

Concessional contributions and defined benefit interests

2.15 Special rules apply to determine concessional contributions for an individual with one or more superannuation interests that are defined benefit interests (broadly, interests where an individual’s entitlement to a benefit is defined by reference to their remuneration or a fixed amount – see section 291-175). This is because contributions to defined benefit schemes may not be directly allocated to individual members. Rather, they are paid into a fund on an aggregate basis from which benefits are paid to members based on their final salary and length of service or other specified factors (rather than just an accumulation of contributions and earnings). Additionally, some defined benefit schemes are wholly or partially unfunded.

2.16 If an individual has a defined benefit interest for an income year, their concessional contributions include the amount of their notional taxed contributions for a financial year in respect of that interest but no other contributions relating to that interest.

2.17 An individual’s notional taxed contributions are determined using the approach set out in Subdivision 291-C of the ITAA 1997 and Subdivision 292-D and Schedule 1A to the *Income Tax Assessment*

Regulations 1997. They are broadly equivalent to the contributions that would have been required in that year to fund the individual's expected final benefits. Notional taxed contributions are only calculated for defined benefit schemes that hold assets and where the schemes are subject to tax. As a result, an individual's notional taxed contributions in respect of a defined benefit interest in an untaxed or unfunded defined benefit scheme are generally nil, and do not reflect the accrued benefit.

2.18 Transitional rules apply in determining an individual's notional taxed contributions for certain defined benefit interests that an individual held on 5 September 2006 or 12 May 2009 respectively. If an individual's notional taxed contributions for such an interest for a financial year would exceed the concessional contributions cap for that year, they will instead be treated as being equal to the cap (see Subdivision 291-C of the (IT(TP)A 1997)).

2.19 For Division 293 tax, an individual's low tax contributions do not include their notional taxed contributions, but instead include their defined benefit contributions. An individual's defined benefit contributions are defined, for most purposes, in Subdivision 293-DA of and Schedule 1AA to the *Income Tax Assessment Regulations 1997*.

2.20 The amount of an individual's defined benefit contributions is generally the same as the amount of their notional taxed contributions for funded defined benefit interests. However, the calculation of defined benefit contributions differs for untaxed or unfunded defined benefit interests. For these types of interests a different method is used that does not rely upon the scheme holding assets and paying tax. As a result, the amount of an individual's defined benefit contributions for such interests generally better reflects the benefits that accrue to the individual.

Summary of new law

2.21 The measure reduces:

- the annual cap applying to concessional contributions made to superannuation to $25,000 (from $30,000 for those aged under 49 at the end of the previous financial year and $35,000 otherwise); and
- the threshold at which high-income earners pay Division 293 tax on their concessionally taxed contributions (otherwise referred to as low tax contributions in this Chapter) to superannuation to $250,000 (from $300,000).

2.22 The measure also amends how concessional contributions are determined to ensure that contributions to constitutionally protected funds and unfunded defined benefit schemes count towards an individual's concessional contributions cap. However, concessional contributions in respect of constitutionally protected funds and unfunded defined benefit schemes by themselves cannot result in a member's concessional contributions cap being exceeded.

Comparison of key features of new law and current law

New law	*Current law*
Annual concessional contributions cap	
The cap on concessional contributions for a financial year is $25,000 for all individuals. The cap is indexed and increases in increments of $2,500 in line with average weekly ordinary time earnings (AWOTE).	The cap on concessional contributions for a financial year is: • $30,000 for individuals aged under 49 years old at the end of the last financial year; and • $35,000 for individuals aged 49 and over at that time. The $30,000 cap is indexed and increases in increments of $5,000 in line with AWOTE.
Division 293 tax threshold	
Division 293 tax applies to an individual for an income year if the total of the individual's combined income for surcharge purposes and concessionally taxed contributions exceeds $250,000.	Division 293 tax applies to an individual for an income year if the total of the individual's combined income for surcharge purposes and concessionally taxed contributions exceeds $300,000.
Concessional contributions – contributions to constitutionally protected funds and defined benefit funds	
Contributions to constitutionally protected funds and untaxed or unfunded defined benefit superannuation funds count towards an individual's concessional contributions cap. The amendments ensure concessional contributions included as a result of these amendments are not treated as excess concessional contributions and subject to tax. However, counting such contributions towards an individual's concessional contributions cap limits their ability to make further concessional contributions. It may result in tax consequences for the individual in relation to their other concessional contributions.	Contributions to constitutionally protected funds do not count towards an individual's concessional contributions cap. The rules for calculating a taxpayer's concessional contributions in respect of their defined benefit interests in untaxed or unfunded superannuation funds often result in the amount of these contributions being zero for the purpose of the concessional contribution cap.

Detailed explanation of new law

2.23 The amendments reform the taxation of concessionally taxed contributions to better target Government support for retirement savings by reducing support for high-income earners through the superannuation system.

Annual concessional contributions cap

Cap amount and indexation

2.24 Schedule 2 to the Bill reduces the cap applying to concessional contributions for a financial year to $25,000 (from $30,000 for those individuals aged under 49 at the end of the previous financial year and $35,000 otherwise). This $25,000 concessional contributions cap applies regardless of an individual's age. ***[Schedule 2, Part 1, items 1 and 16, paragraph 291-20(2)(a) of the ITAA 1997 and Subdivision 291-B of the IT(TP)A 1997]***

2.25 The amount of the concessional superannuation contributions cap is set at $25,000 for the 2017-18 financial year. It continues to be subject to annual indexation under Subdivision 960-M in later years (subject to rounding - see below). Indexation applies to the cap for the financial year in accordance with the growth in the annual rate of full-time AWOTE. ***[Schedule 2, Part 1, item 1, paragraph 291-20(2)(b)]***

2.26 Increases in the cap as a result of indexation are rounded down in increments. The amendments lower the increments at which the cap is increased as a result of indexation. Prior to the amendments, increases in the cap were rounded down to the nearest multiple of $5,000. Schedule 2 to the Bill amends the indexation rules so that increases are instead rounded down to the nearest multiple of $2,500, resulting in more frequent increases. Accordingly, the cap increases only once indexation results in the threshold equalling or exceeding a multiple of $2,500. ***[Schedule 2, Part 1, item 9, 13 and 14, subsections 960-285(1A) and (3A)]***

Example 2.1: Concessional contributions cap

During the 2017-18 income year, concessional contributions made by Oliver and his employer to Oliver's superannuation fund total $28,000. The concessional contributions cap is $25,000. Oliver's concessional contributions exceed this cap. Accordingly, Oliver has concessional contributions of $25,000 and excess concessional contributions of $3,000.

The $3,000 is included in Oliver's assessable income and taxed at his marginal tax rate. Consistent with the prior law, Oliver can elect to withdraw up to 85 per cent of these excess contributions (the amount less the 15 per cent tax already paid by the fund), or retain the full

amount in the superannuation system. He also receives a tax offset equal to 15 per cent of the contribution, to compensate for the tax paid by his superannuation fund. Any excess concessional contribution amount retained in superannuation will be a non-concessional contribution and count towards Oliver's annual non-concessional contributions cap.

Division 293 tax on high-income earners

2.27 Schedule 2 to the Bill reduces to $250,000 (from $300,000) the threshold at which high-income earners pay Division 293 tax on their concessionally taxed contributions. The threshold continues to be based on the total of an individual's income for surcharge purposes for an income year (within the meaning of the income tax law) and their low tax contributions for the corresponding financial year. The amendments do not change the method for calculating these amounts other than the change to the level of the threshold. ***[Schedule 2, Part 2, item 25, subsection 293-20(1)]***

Example 2.2: Division 293 tax

During the 2017-18 income year, the sum of Tegan's income for surcharge purposes and her low tax contributions is $295,000. Tegan is therefore required to pay an amount of tax under Division 293.

Tegan exceeded the $250,000 threshold by $45,000 ($295,000 less $250,000). Tegan's low tax contributions for 2017-18 are $25,000. Therefore her taxable contributions are $25,000, being the lesser of these two amounts.

The Division 293 tax is applied at a rate of 15 per cent to Tegan's taxable contributions of $25,000. Accordingly, Tegan is required to pay $3,750 in Division 293 tax for the 2017-18 income year.

Concessional contributions – contributions to constitutionally protected funds and defined benefit funds

2.28 Schedule 2 to the Bill better targets government support for retirement savings by amending the income tax law to count contributions to constitutionally protected funds and unfunded defined benefit schemes towards an individual's concessional contributions cap. The amendments also ensure concessional contributions included as a result of these amendments are not treated as excess concessional contributions and subject to tax. However, counting such contributions towards an individual's concessional contributions cap limits their ability to make further concessional contributions. It may result in tax consequences for the individual in relation to their other concessional contributions.

Contributions to constitutionally protected funds

2.29 Schedule 2 to the Bill makes amendments to treat a contribution (including a notional contribution) to a constitutionally protected fund as a concessional contribution within the meaning of the ITAA 1997.

2.30 This is achieved by removing contributions to constitutionally protected funds from the category of contributions that are specifically treated as not being concessional contributions. Further to this, a contribution to a constitutionally protected fund is treated as forming part of assessable income solely for the purposes of determining if it is a concessional contribution (see paragraph 291-25(2)(b)). Such contributions would otherwise not be concessional contributions because constitutionally protected funds do not have assessable income. These amendments do not remove the existing income tax exemption for constitutionally protected funds provided by table item 5.3 in section 50-25. ***[Schedule 2, Part 1, items 2 and 3, paragraph 291-25(2)(c) and subsection 291-25(4)]***

2.31 Prior to these amendments, a contribution (including a notional contribution to a defined benefit superannuation interest) did not count towards the member's concessional contributions cap if it was made to a constitutionally protected fund. This allowed members of constitutionally protected funds to receive or accrue any amount of employer contributions and other contributions to such funds without affecting their ability to have concessional contributions made to other superannuation interests.

2.32 These amendments remove this advantage by treating such contributions to constitutionally protected funds as concessional contributions.

Concessional contributions – rules for defined benefit interests

2.33 Schedule 2 to the Bill amends the rules for calculating a member's concessional contributions for a financial year in respect of a defined benefit interest. The amendments ensure that the calculation of notional amounts representing contributions to unfunded defined benefit schemes more closely reflects the value of a member's accrued benefits. The amendments ensure individuals with such superannuation interests are not unduly advantaged in saving for retirement.

2.34 The amendments provide that a taxpayer's concessional contributions for a financial year in respect of a defined benefit interest (including a defined benefit interest in a constitutionally protected fund) includes the amount by which the taxpayer's defined benefit contributions exceed their notional taxed contributions. This amount is intended to be a proxy for contributions that would have been needed to support unfunded

defined benefits scheme interests accrued for that financial year. A member's concessional contributions for a financial year will still include the amount of their notional taxed contributions in respect of such interests, as well as any amounts in respect of interests that are not defined benefit interests currently required to be included (see paragraphs 291-165(a) and (b)). ***[Schedule 2, Part 1, items 4 to 7, paragraph 291-165(1)(c), subsection 291-160(2) and sections 291-160 and 291-165]***

2.35 An individual's defined benefit contributions are defined, for most purposes, in Subdivision 293-DA and Schedule 1AA to the *Income Tax Assessment Regulations 1997* (see paragraphs 2.19 to 2.20 above for more information). For the purposes of working out the individual's defined benefit contributions for a financial year, certain modifications to the meaning of defined benefit contributions must be disregarded. These modifications reduce these contributions to nil for most contributions to constitutionally protected funds and to interests established under the *Judges' Pensions Act 1968* in subsections 293-150(3) and 293-195(2). These modifications must be disregarded as such amounts are not intended to be treated as nil for the purpose of the concessional contributions cap. ***[Schedule 2, Part 1, item 7, subsection 291-165(2)]***

Capping the value of newly included concessional contributions

2.36 The amendments (described in paragraphs 2.29 to 2.35 above) are designed to ensure that contributions (including notional contributions) to constitutionally protected funds and untaxed or unfunded superannuation funds count towards an individual's concessional contributions cap. This limits the ability of the individual to make further concessional contributions to other funds and ensures they are treated more consistently with individuals that are not members of such funds.

2.37 As these amendments are not designed to subject such contributions to tax (noting their tax treatment in the end benefits stage), these amendments limit the impact that including these amounts as concessional contributions would otherwise have on an individual's tax position. The amendments also ensure that the interaction between these amendments and the transitional rules (described in paragraph 2.18 above) does not result in unintended outcomes.

2.38 The amendments achieve this by providing that the sum of the following amounts are treated as equal to an individual's concessional contributions cap for the financial year if they would otherwise exceed that cap for that year:

- their contributions (including notional contributions in respect of defined benefit interests) for the financial year to a

constitutionally protected fund (see paragraphs 2.29 to 2.35 above);

- their notional taxed contributions covered by the 2006 or 2009 transitional arrangements (see section 291-170 of the IT(TP)A 1997– refer to paragraph 2.18 above); and
- the amount (if any) by which their defined benefit contributions (other than contributions covered by the first circumstance above) for the financial year exceeds their notional taxed contributions for the financial year (see paragraphs 2.33 to 2.35 above).

[Schedule 2, Part 1, item 8, subsections 291-370(1) and (2)]

2.39 Concessional contributions made in excess of the concessional contributions cap would otherwise be treated as excess concessional contributions. Excess concessional contributions are included in the assessable income of the individual (with a tax offset provided to account for the tax expected to have been paid by the fund). The individual may either elect to withdraw such contributions from the superannuation fund or retain the contributions as non-concessional contributions (sections 291-15 and 292-90 of the ITAA 1997 and Division 95 of Schedule 1 to the *Taxation Administration Act 1953*). They may also be subject to the excess concessional contribution charge (Division 95 of Schedule 1 to the *Taxation Administration Act 1953*). These amendments ensure that such contributions do not result in excess concessional contributions and therefore do not have these tax consequences.

2.40 The amendments prevent any combination of the contributions described in paragraph 2.38 above by themselves causing the individual’s concessional contributions for a financial year to exceed the concessional contributions cap. For the purpose of these amendments, the concessional contributions cap is $25,000 (indexed annually) (see paragraphs 2.24 and 2.26 above). ***[Schedule 2, Part 1, item 8, subsection 291-370(1)]***

Example 2.3: Contributions to constitutionally protected fund and unfunded defined benefit interest

Marvin has concessional contributions to a constitutionally protected fund of $20,000 for the 2017-18 financial year. Marvin also has defined benefit contributions of $22,000 and notional taxed contributions for that financial year of $18,000 in respect of certain defined benefit interests (which are not interests in a constitutionally protected fund). The difference between Marvin's defined benefit contributions and his notional taxed contributions ($4,000) represents contributions in respect of unfunded defined benefit interests.

Prima facie, Marvin's total concessional contributions for the financial year are equal to $42,000. This is worked out by applying the rules introduced by these amendments and the current law, which provide that Marvin's concessional contributions are the sum of his contributions to constitutionally protected funds, his notional taxed contributions and the difference between his defined benefit contributions and his notional taxed contributions ($20,000 + $18,000 + ($22,000 - $18,000)).

However, as the sum of these amounts (which are all covered by section 291-370) exceeds the concessional contributions cap of $25,000, section 291-370 applies to treat the sum of these contributions as equal to the concessional contributions cap. Therefore rather than having concessional contributions of $42,000, Marvin is treated as having concessional contributions of $25,000. Hence, Marvin does not exceed the concessional contributions cap for the 2017-18 financial year.

However, when benefits are paid from Marvin's constitutionally protected fund and his unfunded defined benefits, they are subject to higher rates of taxation than his benefits paid from a taxed source.

2.41 Including amounts covered by the transitional rules described at paragraph 2.18 above, ensures that notional taxed contributions that are covered by the 2006 or 2009 transitional arrangements will not be subject to excess contributions tax. For the purpose of these amendments, amounts are covered by the transitional rules where:

- section 291-170 of the IT(TP)A 1997 applies to treat their notional taxed contributions as equal to their concessional contributions cap; or
- section 291-170 of the IT(TP)A 1997 does not apply but would apply had the taxpayer's notional taxed contributions exceeded their concessional contributions cap (see paragraph 291-170(2)(b) of IT(TP)A 1997).

2.42 The following example illustrates how including these amounts prevents an anomalous outcome arising from the interaction between these transitional rules and the cap for concessional contributions now included by these amendments. ***[Schedule 2, Part 1, item 8, paragraph 291-370(1)(b)]***

Example 2.4: Interaction between transitional cap and cap for newly included concessional contributions

Anh has notional taxed contributions of $26,000 for the 2017-18 income year to a defined benefit superannuation interest which are covered by the transitional rules in section 291-170 of IT(TP)A 1997. Anh also has contributions to a constitutionally protected fund of $27,000.

Under section 291-170 of IT(TP)A 1997, Anh's notional taxed contributions are treated as equal to her concessional contributions cap (that is, $25,000), as $26,000 exceeds this cap. Therefore prima facie, Anh's concessional contributions are equal to $52,000. This is worked out by adding her notional taxed contributions calculated under section 291-170 of IT(TP)A 1997 to her contributions to constitutionally protected funds ($25,000 + $27,000).

However, as the sum of these amounts (which are all amounts covered by section 291-370) exceeds the concessional contributions cap of $25,000, section 291-370 applies to treat the sum of these contributions as equal to the concessional contributions cap. Therefore rather than having concessional contributions of $52,000, Anh is treated as having concessional contributions of $25,000.

If these amendments did not apply to include amounts capped under the transitional rules, Anh's notional taxed contributions would be treated as equal to $25,000 under section 291-170 of IT(TP)A 1997 and these amendments would treat the $27,000 of contributions to the constitutionally protected fund as equal to $25,000. Therefore Anh would have had concessional contributions of $50,000 (twice the concessional contributions cap). The amendment ensures this outcome does not occur.

2.43 The amendments do not prevent a taxpayer from exceeding their concessional contributions cap as a result of having contributions other than those described in paragraph 2.38 above (uncapped contributions), or as a result of having some combination of uncapped contributions and contributions described in paragraph 2.38 above (capped contributions).

2.44 The following examples illustrate situations where an individual can exceed their concessional contributions cap as a result of having a combination of uncapped and capped contributions.

Example 2.5: Contributions to unfunded defined benefit fund and accumulation fund

Ruby has a defined benefit interest in an unfunded superannuation fund. Her defined benefit contributions in respect of the fund for the 2017-18 financial year exceed her notional taxed contributions for the financial year by $30,000. This gives her a capped contribution amount of $30,000.

Ruby also makes concessional contributions of $15,000 in the same financial year to a superannuation fund (that is not a constitutionally protected fund) in which she has an accumulation interest. This gives her an uncapped contribution amount of $15,000.

Her capped contributions exceed the concessional contributions cap of $25,000. However, the amendments treat these contributions as being equal to the concessional contributions cap of $25,000. The total of Ruby's additional contributions to her accumulation interest of $15,000 is therefore treated as being in excess of her concessional contributions cap. Accordingly, these are excess concessional contributions.

Example 2.6: Contributions to unfunded defined benefit fund and accumulation fund

Assume the same facts as Example 2.5 except that Ruby's defined benefit contributions exceed her notional taxed contributions for the financial year by $20,000. This gives her a capped contribution amount of $20,000.

As Ruby also makes uncapped superannuation contributions of $15,000 her total concessional contributions are treated as being $35,000. Accordingly, contributions of $10,000 are treated as being in excess of her concessional contributions cap and are excess concessional contributions.

Consequential amendments

Concessional contributions annual cap and Division 293 tax

General

2.45 Schedule 2 to the Bill makes a number of consequential amendments to the income tax law, the *Taxation Administration Act 1953*, and the *Superannuation Guarantee (Administration) Act 1992*. ***[Schedule 2, Part 1, items 4, 8, 10 to 12 and 15, sections 291-60, 291-365, subsections 960-285(2) and (4), Part 2, items 21 to 26, sections 293-1, 293-5, 293-10 and subsections 293-155(1) and***

293-200(1) of the ITAA 1997 and the note to subsection 133-15(1) in Schedule 1 to the Taxation Administration Act 1953]

Maximum contribution base

2.46 Part 3 of Schedule 2 also amends how the maximum contribution base is determined under the *Superannuation Guarantee (Administration) Act 1992*.

2.47 The maximum contribution base is the cap on the amount of an employee's salary and wages that is taken into account in determining an employer's liability for the superannuation guarantee charge for a quarter. In effect, employers do not need to make mandatory superannuation contributions in relation to the amount of an employee's ordinary time earnings that exceeds the maximum contribution base.

2.48 The maximum contribution base is $51,620 per quarter in the 2016-17 financial year. Accordingly, the effective cap on contributions required to avoid being subject to the superannuation guarantee charge for a quarter in the 2016-17 financial year is $4,903.90 (i.e. the maximum contribution base multiplied by the charge percentage for the quarter divided by 100 or $51,620 multiplied by 0.095). Extended over an income year, this would result in annual contributions for 2016-17 totalling $19,615.60.

2.49 Indexation of the new concessional contributions cap under these amendments is subject to different rounding rules than the maximum contribution base. This will result in the contributions required for an employee with ordinary time earnings equal to or more than the maximum contribution base exceeding the concessional contributions cap within a number of years. The amendments ensure that mandatory employer contributions cannot by themselves result in employees having excess concessional contributions.

2.50 To address this issue, Part 3 of Schedule 2 provides that if the maximum contribution base for a quarter effectively requires contributions to be made that, if paid over the year, would result in the employee's concessional contributions exceeding the concessional contribution cap, the maximum contribution base is instead reduced to the amount that would not result in excess concessional contributions. This is determined by the following formula:

$$\textbf{Concessional contributions cap} \times \frac{\textbf{100}}{\textbf{charge percentage}} \times \frac{\textbf{1}}{\textbf{4}}$$

[Schedule 2, Part 3, item 28, subsections 15(5) and (6) of the Superannuation Guarantee (Administration) Act 1992]

2.51 As a result of this change, an employer will not be subject to the superannuation guarantee charge if they do not make contributions that would be excess concessional contributions for an employee. With the new concessional contributions cap and charge percentage as at 1 July 2017, this would occur if the maximum contribution base for the quarter is greater than $65,789.47.

2.52 This change to the maximum contribution base affects whether an employer will be subject to the superannuation guarantee charge if they do not make superannuation contributions or sufficient contributions for an employee. It does not limit employers from making contributions or alter the terms of an employee's remuneration.

Concessional contributions – contributions to constitutionally protected funds and defined benefit funds

2.53 These amendments include guidance material for Subdivision 291-CA of the ITAA 1997 and notes to assist users of the legislation. ***[Schedule 2, Part 1, items 7, 8, 17 and 18, section 291-165 of the ITAA 1997 and subsections 291-170(2) and (4) of the IT(TP)A 1997]]***

2.54 These amendments ensure that the 2006 or 2009 transitional arrangements (described at paragraph 2.18 above) do not apply in relation to a defined benefit interest in a constitutionally protected fund. ***[Schedule 2, Part 1, item 19, subsection 291-170(6) of the IT(TP)A 1997]***

Application and transitional provisions

2.55 The amendments in Schedule 2 to the Bill commence on the first day of the first quarter after Royal Assent. ***[item 2 in the table in section 2 of the Bill]***

2.56 Part 1 of Schedule 2 to the Bill applies in relation to superannuation contributions made on or after 1 July 2017. ***[Schedule 2, Part 1, item 20]***

2.57 Part 2 of Schedule 2 to the Bill applies in relation to the 2017-18 income year and later income years. ***[Schedule 2, Part 2, item 27]***

Chapter 3
Annual non-concessional contributions caps

Outline of chapter

3.1 An exposure draft Bill and Explanatory Material for this measure will be released in the coming weeks.

Chapter 4
Low income superannuation tax offset

Outline of chapter

4.1 An exposure draft Bill and Explanatory Material for this measure was released for public consultation on 7 September 2016.

Chapter 5
Deducting personal contributions

Outline of chapter

5.1 An exposure draft Bill and Explanatory Material for this measure was released for public consultation on 7 September 2016.

Chapter 6
Catch-up concessional contributions

Outline of chapter

6.1 The exposure draft of Schedule 6 to the Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (the Bill) introduces provisions to allow catch-up concessional contributions. This will allow individuals to make additional concessional superannuation contributions in a financial year by utilising unused concessional contribution cap amounts from up to five previous years, providing that their total superannuation balance at 30 June of the previous financial year was below $500,000.

6.2 All references in this Chapter are to the *Income Tax Assessment Act 1997* unless otherwise specified.

Context of amendments

6.3 This measure forms part of the Government's Superannuation Reform Package announced in the 2016-17 Budget. It will enhance the flexibility and accessibility of the superannuation system for individuals who take time out of work, work part-time or have 'lumpy' income (for example small business operators), by allowing them to make catch-up concessional contributions.

6.4 Annual concessional contributions caps can limit the ability of people with interrupted work patterns or irregular incomes to accumulate superannuation balances commensurate with those who do not take breaks from the workforce. Allowing people to carry forward unused concessional contributions cap amounts for a period of up to five years will provide them with the opportunity to 'catch-up' if they have the capacity and choose to do so.

6.5 The measure also ensures that only those people who have not had the capacity to contribute up to their concessional contributions cap in prior years will be able to make catch-up contributions by targeting it to those individuals who have been unable to accumulate large superannuation balances.

6.6 Prior to these amendments individuals who could not fully utilise their annual concessional contributions cap in a financial year could

not carry forward unused concessional contributions cap amounts to another financial year.

6.7 Schedule 6 to the Bill will allow individuals with total superannuation balances of less than $500,000 at the end of a financial year to make additional concessional contributions in the next financial year by allowing them to access unused concessional contribution cap amounts from the previous five financial years. Unused cap amounts can be carried forward from the 2018-19 financial year.

6.8 Related measures in the Government's 2016-17 Budget Superannuation Reform Package will reduce the annual cap on concessional superannuation contributions to $25,000 and allow all individuals under 65 (and those between 65 and 74 who meet a work test) to make deductible personal contributions to superannuation.

Summary of new law

6.9 Schedule 6 to the Bill will allow individuals with a total superannuation balance of less than $500,000 at the end of a financial year to make additional concessional contributions in the next financial year by accessing unused concessional contribution cap amounts carried forward from the previous five years.

6.10 An individual's total superannuation balance includes the value of their superannuation interests in the accumulation phase, the balance of their transfer balance account (adjusted for the value of the individual's interests in account-based income streams in the retirement phase), and 'in transit' rolled-over superannuation benefits.

Comparison of key features of new law and current law

New law	*Current law*
Increased concessional contributions cap	
Individuals with a total superannuation balance of less than $500,000 on 30 June of the previous financial year can increase their concessional contributions cap in the next financial year by applying unused concessional contributions cap amounts from one or more of the previous five financial years. An individual can carry forward unused concessional contributions cap amounts from the 2018-19 financial year onwards.	There is an annual cap on the amount of concessional contributions made in respect of an individual for a given financial year. An individual has excess concessional contributions for a financial year if their concessional contributions for the year exceed their concessional contributions cap for the year. If an individual does not use the entire amount of their concessional contributions cap in a financial year they are not able to carry forward unused amounts.
Total superannuation balance	
An individual's total superannuation balance at a particular time is the sum of: • the accumulation phase value of their superannuation interests that are not in the retirement phase; • the balance of their transfer balance account (disregarding debits and credits to the account for interests in account based income streams and adding back the current value of the individual's interests in account based income streams in the retirement phase); • any amount rolled over between funds before that time, but not received until after that time, that is not reflected in the individual's accumulation phase value or balance of their transfer balance account.	No equivalent.

Detailed explanation of new law

6.11 Schedule 6 to the Bill amends Division 291 to allow individuals who have a total superannuation balance of less than $500,000 on 30 June of the previous financial year to increase their concessional contributions cap in the next financial year if they have unused concessional contributions cap amounts from the previous five financial years.

Background

6.12 Division 291 places an annual cap on the amount of superannuation contributions that may receive concessional tax treatment for an individual in a financial year. Concessional superannuation contributions are broadly those that are made to a complying superannuation provider by an employer on behalf of an individual or by the individual themselves, which are included in the assessable income of the superannuation provider in relation to the plan and in respect of which the employer or individual claims an income tax deduction.

6.13 Concessional contributions that exceed the annual cap are excess concessional contributions. An amount equal to the excess is included in an individual's assessable income with a tax offset to compensate for income tax already applied to the contributions in the superannuation fund.

Five year carry forward of unused concessional contributions cap

6.14 Schedule 6 to the Bill introduces provisions to allow a five year carry forward of unused concessional contributions cap amounts. An individual will be able to make additional concessional contributions in a financial year using these carried forward amounts if:

- their concessional contributions for the year would otherwise exceed the concessional contributions cap for that year; and
- they had a total superannuation balance of less than $500,000 on 30 June of the previous financial year; and
- they have unused concessional contributions cap amounts from one or more of the previous five financial years. ***[Schedule 6, Part 1, items 1 to 4, subsections 280-15(1) and (2), section 291-1 and subsections 291-20(3))]***

Unused concessional contributions cap

6.15 An individual has unused concessional contributions cap for a financial year if they did not fully utilise their concessional contributions

cap that year. The amount of the unused concessional contributions cap is the difference between the individual's concessional contributions and the concessional contributions cap. ***[Schedule 6, Part 1, item 4 and 5, subsections 291-20(6) and 995-1(1)]***

6.16 However, an individual cannot have unused concessional contributions cap for a financial year earlier than the 2018-19 financial year. This means that the first year in which an individual will be able to make additional concessional contributions by applying their unused concessional contributions cap amounts is the 2019-20 financial year. ***[Schedule 6, Part 1, item 4, subsection 291-20(7)]***

Increased concessional contributions cap

6.17 If an individual makes concessional contributions that exceed the concessional contributions cap they can increase their concessional contributions cap. To do so they must have a total superannuation balance of less than $500,000 on 30 June of the previous financial year and have unused concessional contributions cap amounts from one or more of the previous five financial years. ***[Schedule 6, Part 1, item 4, subsection 291-20(3)]***

6.18 However, an individual's concessional contributions cap cannot be increased by more than the amount by which they would otherwise exceed the concessional contributions cap. That is, only the exact amount of unused concessional contributions cap that is necessary is used, and any remaining unused concessional contributions cap is preserved and continues to carry forward. ***[Schedule 6, Part 1, item 4, subsection 291-20(4)]***

6.19 Amounts of unused concessional contributions cap are applied to increase an individual's concessional contributions cap in order from the earliest year to the most recent year. ***[Schedule 6, Part 1, item 4, subsection 291-20(5)]***

6.20 Unused concessional cap amounts not utilised after five years will no longer be able to be carried forward.

Example 6.1: Unused concessional contributions cap

In the 2018-19 financial year Layla's employer made concessional superannuation guarantee contributions of $10,000 on her behalf to her superannuation fund. Layla did not make any deductible personal contributions to her fund.

The concessional contributions cap for the 2018-19 financial year is $25,000.

Layla's unused concessional contributions cap amount for the 2018-19 financial year is therefore $15,000.

Example 6.2: Increased concessional contributions cap

Between the 2018-19 and 2022-23 financial years Layla's concessional contributions and unused concessional contributions cap are as follows:

	2018-19	***2019-20***	***2020-21***	***2021-22***	***2022-23***	***2023-24***
Concessional contributions	$10,000	$10,000	$10,000	$10,000	$10,000	$40,000
Available unused cap	$15,000	$15,000	$15,000	$15,000	$15,000	$0

In the 2023-24 financial year Layla makes a deductible personal contribution of $30,000 in addition to her employer's concessional superannuation guarantee contribution of $10,000 on her behalf. On 30 June 2023 Layla had a total superannuation balance of less than $500,000. Assuming the concessional contributions cap is $25,000 (for all years between 2018-19 and 2023-24), Layla will have exceeded this cap by $15,000. However, Layla will be able to increase her concessional contributions cap for the 2023-24 financial year by using $15,000 of unused concessional contributions cap from the 2018-19 financial year.

Example 6.3: Increased concessional contributions cap

Further to Example 6.2, in the 2024-25 financial year Layla makes a deductible personal contribution of $20,000 in addition to her employer's concessional superannuation guarantee contribution of $10,000 on her behalf. On 30 June 2024 Layla's total superannuation balance was still less than $500,000.

	2019-20	***2020-21***	***2021-22***	***2022-23***	***2023-24***	***2024-25***
Concessional contributions	$10,000	$10,000	$10,000	$10,000	$40,000	$30,000
Available unused cap	$15,000	$15,000	$15,000	$15,000	$0	$0

Assuming the concessional contributions cap is $25,000, Layla will have exceeded this cap by $5,000. However, Layla will be able to increase her concessional contributions cap for the 2024-25 financial year by using $5,000 of her unused concessional contributions cap from the 2019-20 financial year.

The remaining $10,000 unused concessional contributions cap from the 2019-20 financial year cannot continue to be carried forward. This is because in the 2025-26 financial year it would be outside of the five year carry forward period.

Example 6.4: $500,000 total superannuation balance

On 30 June 2021 Jason had a total superannuation balance of $480,000 and unused concessional contribution cap amounts from the previous three financial years. He is therefore eligible to make an additional concessional contribution in the 2021-22 financial year.

In the 2021-22 financial year Jason uses his unused concessional contributions cap amounts to make additional concessional contributions of $45,000, on top of his employer's concessional superannuation guarantee contribution of $5,000. In order to do so, he uses up the full amount of his unused concessional contributions cap from the 2018-19 and 2019-20 financial years, plus $5,000 from the 2020-21 financial year.

	2018-19	2019-20	2020-21	2021-22
Concessional contributions	$5,000	$5000	$5000	$50,000
Available unused cap	$20,000	$20,000	$20,000	$0
Remaining unused cap space available for carry forward	$0	$0	$15,000	$0

On 30 June 2022 Jason now has a total superannuation balance of $530,000. This means that Jason will not be able to increase his concessional contributions cap using unused concessional contribution cap amounts in the 2022-23 financial year.

However, if Jason's total superannuation balance later reduces below $500,000 he will again be eligible to increase his concessional contributions cap by accessing his unused concessional contribution cap amounts from the five years prior to the year that he is now eligible to make further contributions.

Total superannuation balance

6.21 Schedule 6 to the Bill introduces the concept of an individual's 'total superannuation balance'. This concept is relevant for several measures announced in the Government's 2016-17 Budget Superannuation Reform Package and ensures the consistent treatment for the valuation of an individual's total superannuation balance across all of these measures.

6.22 An individual's total superannuation balance, at a particular time, is the sum of the following:

- the accumulation phase value of a superannuation interest that is not in the retirement phase at that time;
- the retirement phase value of a superannuation interest which is the balance of a transfer balance account at that time (but not less than nil) adjusted to reflect the current value of account based superannuation interests in the retirement phase; and
- the amount of each roll-over superannuation benefit paid at or before that time, that is received after that time, and not reflected in the accumulation phase value of a superannuation interest or the retirement phase value of a superannuation interest. ***[Schedule 6, Part 2, items 9 and 10, section 307-230, subsection 995-1(1)]***

Accumulation phase value

6.23 The default rule for determining the accumulation phase value of an individual's superannuation interest at a particular time will be the total amount of superannuation benefits that would become payable if the individual voluntarily caused the interest to cease at that time. Otherwise the accumulation phase value will be the value of the superannuation interest as set out in the *Income Tax Assessment Regulations 1997*. ***[Schedule 6, Part 2, items 7, 8, 10 and 11, paragraph 307-205(2)(b) and subsection 995-1(1)]***

6.24 Where an individual had a single superannuation interest in a superannuation entity regulated under the *Superannuation Industry (Supervision) Act 1993* this amount would be a member's withdrawal benefit, which is the amount of benefits that would be payable to the member, and/or rolled over to another superannuation fund or retirement savings account, if the member voluntarily ceased to be a member of the fund.

6.25 However, if a member has more than one superannuation interest in a given superannuation entity it would be possible for a member to cease an interest in the entity but still retain membership of the entity in respect of other interests. For example a member, on resignation from employment, could be entitled to be paid a defined benefit income stream (with no lump sum equivalent) and also have an accumulation account balance, from their fund. In these circumstances, only the value of the accumulation account would be included in the accumulation value.

6.26 The regulation making power will enable alternative valuation rules to be prescribed for certain types of superannuation interests, or superannuation interests in specific funds, in circumstances where the

default rule could lead to a nil or minimal valuation. ***[Schedule 6, item 8, paragraph 307-205(2)(a)]***

6.27 The above amendments require a minor, consequential amendment to be made to subregulations 307-205.01(1) and 307-205.02(1) of the *Income Tax Assessment Regulations 1997* to update legislative references. ***[Schedule 4, item 1, subregulations 307-205.01(1) and 307-205.02(1) of the Income Tax Assessment Regulations 1997]***

Retirement phase value

6.28 The retirement phase value of an individual's total superannuation balance is determined by the balance of their transfer balance account, adjusted to reflect the current value of account based superannuation interests in the retirement phase. ***[Schedule 6, Part 2, item 9, paragraph 307-230(1)(b) and subsections 307-230(2) and (3)]***

6.29 Using this method will ensure that an individual's total superannuation balance is as up-to-date as possible without imposing an additional obligation on superannuation income stream providers to calculate other superannuation interest balances, for example for defined benefit interests, on an annual basis, as these interests have already been calculated for the purposes of the transfer balance account.

6.30 Schedule 1 to the Bill introduces the concept of a 'transfer balance account'. This account represents the net amount of capital an individual has transferred to their superannuation retirement phase.

6.31 The balance of an individual's transfer balance account will generally be the commencement value of a superannuation income stream that is in the retirement phase.

6.32 An individual's transfer balance account will be debited in limited circumstances. It is possible for an individual's transfer balance account to have a negative balance if their debits exceed their credits. However, for the purposes of the total superannuation balance, the transfer balance account cannot be less than nil.

6.33 The balance of an individual's transfer balance account will be adjusted for the purposes of working out their total superannuation balance to reflect the actual value of an interest in an account-based income stream at a particular time. All other superannuation income stream interests will retain the value for the given interest attributed to the transfer balance account. ***[Schedule 6, Part 2, item 9, subsections 307-230(2) and (3)]***

6.34 The adjustment to the transfer balance account balance will disregard certain credit and debit amounts made to the account for

superannuation interests that support an account-based superannuation income stream. The account balance of the income stream, being the value of the interest in the income stream if it is voluntarily ceased or is deemed to cease at that time, is then added back to the transfer balance account. The adjustment provisions will cover all superannuation income streams for which there is an account balance attributable to a beneficiary being allocated, account-based or market linked pensions and annuities. ***[Schedule 6, Part 2, item 9, subsections 307-230(2) and (3)]***

6.35 A regulation will be made to set out the meaning of an account-based annuity in the *Superannuation Industry (Supervision) Regulations 1994.* ***[Schedule 6, Part 2, item 10, subsection 995-1(1)]***

6.36 For further detail on the concept of transfer balance account, see Chapter 1.

Roll-over superannuation benefit

6.37 The third component of the total superannuation balance is an individual's roll-over superannuation benefit that is paid at or before that time, which is received after that time, and not reflected in the individual's accumulation phase value or balance of the transfer balance account. ***[Schedule 6, Part 2, item 9, paragraph 307-230(1)(c)]***

6.38 This limb is intended to capture amounts that are rolled-over at the end of a financial year that would not otherwise be accounted for in the accumulation phase value of an individual's superannuation interest at a particular time because the amount is 'in transit'.

Example 6.5: Roll-over superannuation benefit

Jennifer has $450,000 in the accumulation phase in her superannuation fund, Fund A.

On 29 June 2019 Jennifer requests Fund A to partially roll-over an amount of $100,000 to Fund B. Fund B does not receive the $100,000 roll-over superannuation benefit until 1 July 2019.

On 30 June 2019, Jennifer's total superannuation balance is the $350,000 remaining in accumulation phase in Fund A plus the $100,000 roll-over superannuation benefit that is in transit to Fund B. This is because the roll-over amount was paid before 30 June 2019 but not received by Fund B until after that time, and it was not reflected in her accumulation phase value which is calculated at 30 June of that year.

Application and transitional provisions

6.39 The amendments made by Schedule 6 commence on the first day of the next quarter following the day of Royal Assent. ***[Item 2 in the table in section 2 of the Bill]***

6.40 Part 1 of Schedule 6 to the Bill applies in relation to working out the concessional contributions cap for the 2019-20 financial year and later financial years. ***[Schedule 6, Part 1, item 6]***

6.41 An amendment made by Part 2 of Schedule 6 to the Bill applies in relation to another amendment in the same way as that amendment applies. For example, Part 2 of Schedule 6 applies in relation to Part 1 of Schedule 6 in the same way as Part 1 applies. ***[Schedule 6, Part 2, item 12]***

Chapter 7
Tax offsets for spouse contributions

7.1 An exposure draft Bill and Explanatory Material for this measure was released for public consultation on 7 September 2016.

Chapter 8
Innovative income streams and integrity

Outline of chapter

8.1 The exposure draft of Schedule 8 to the Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (the Bill) amends the earnings tax exemptions in the *Income Tax Assessment Act 1997* (ITAA 1997) to:

- extend the earnings tax exemption to new lifetime products such as deferred products and group self-annuities;
- remove the earnings tax exemption in respect of transition to retirement income streams (TRISs); and
- introduce an integrity measure that will apply to self-managed superannuation funds (SMSFs) and small Australian Prudential Regulation Authority (APRA) funds to support the operation of the transfer balance cap measure.

8.2 For the purposes of this Chapter, references to a TRIS will generally also include a transition to retirement income pension (TRIP), a non-commutable allocated pension and a non-commutable allocated annuity.

8.3 All references in this Chapter are to the ITAA 1997 unless otherwise specified.

Context of amendments

8.4 The Government's 2016-17 Budget Superannuation Reform Package included measures to enhance the flexibility and integrity of the superannuation system. These measures will:

- remove tax barriers to the development of innovative income stream products by extending the earnings tax exemption to new lifetime products such as deferred products and group self-annuities;
- strengthen the integrity of superannuation income streams by removing the earnings tax exemption in respect of TRISs; and

- prevent SMSFs and small APRA funds, where one or more members have a superannuation interest in the retirement phase and a total superannuation balance of over $1.6 million from using the segregated assets method to calculate earnings tax exemptions.

8.5 These measures seek to balance the integrity of the superannuation reform package, while maintaining the flexibility for trustees to operate their funds and manage funds' compliance costs.

Innovative retirement income products

8.6 In May 2016 the Government announced its response to the Retirement Income Streams Review and released its final report as part of the 2016-17 Budget.

8.7 The Government announced that it would remove tax barriers to the development of new retirement income products by extending the earnings tax exemption to new lifetime products such as deferred products and group self-annuities.

8.8 Currently, the earnings tax exemption provisions do not cover deferred products that may delay the commencement of annuity or pension payments for a number of years. This reflects the current annuity and pension standards in the *Superannuation Industry (Supervision) Regulations 1994* (SISR 1994) that require all superannuation income streams to make an annual superannuation benefit payment. These standards limit opportunities for individuals to better manage consumption and longevity risk in retirement.

8.9 Related regulations will amend the annuity and pension standards in the SIS Regulations to facilitate the development of new innovative retirement income products including deferred products and group self-annuities.

Transition to retirement income streams

8.10 The SISR 1994 and the *Retirement Savings Accounts Regulations 1997* (RSAR 1997) currently permit individuals who have reached preservation age, but not retired from the workforce or attained age 65, to draw down their pension or annuity through commencing a TRIS, a transition to retirement income pension (TRIP) or a non-commutable allocated pension or non-commutable allocated annuity.

8.11 Non-commutable allocated pensions and non-commutable allocated annuities are old-style TRISs that were offered by superannuation funds between 1 July 2005 and 20 September 2007.

8.12 TRISs were intended to assist older individuals transition to retirement by supplementing reduced income from decreased working hours with payments from a superannuation income stream. However, they have also been used for the sole purpose of achieving tax advantages. For example, individuals can salary sacrifice income into superannuation and draw down their account balance by commencing a TRIS to receive income taxed at a concessional rate but not reduce their working hours. Further, individuals may elect to treat superannuation income stream benefits as lump sums, which are tax-free up to the low rate cap of $195,000.

8.13 Related regulations will remove this election in regulation 995-01.03 so that individuals are no longer able to treat superannuation income stream benefits as superannuation lump sums.

Excluding SMSFs and small APRA funds with members with large balances from segregating assets

8.14 The introduction of the transfer balance cap will mean that some individuals will be required to reduce the value of their interests in the retirement phase to $1.6 million. Most will rollback some or all of their excess to the accumulation phase. If funds with members in both the pension and accumulation phase use the segregated assets method to determine their earnings tax exemption, assets can be cycled between the segregated pools for each phase to avoid capital gains tax.

8.15 These funds will now be required to use the proportioning method to determine their earnings tax exemption.

Summary of new law

8.16 Schedule 8 to the Bill amends the earnings tax exemption provisions of the ITAA 1997 that treat income earned from assets that fund current pension liabilities as exempt income of a complying superannuation fund, RSA provider or life insurance company.

8.17 The earnings tax exemption will be extended to new innovative retirement income products that are deferred superannuation income streams (including guaranteed annuities and group self-annuities) and will no longer be available in respect of TRISs.

8.18 In order to implement these changes, the earnings tax exemption provisions are reframed so that they no longer refer to superannuation income stream benefits that are payable at the time. Instead, the earnings tax exemption will be applied when a superannuation income stream is in the 'retirement phase' at the time.

8.19 A superannuation income stream will be in the retirement phase at a time if:

- a superannuation income stream benefit is payable from it at the time; or
- in the case of a deferred superannuation income stream — a superannuation income stream benefit is payable at a later time and the person who will receive the benefit has satisfied a relevant nil condition of release.

8.20 However, a superannuation income stream will not be in the retirement phase if it is a TRIS.

8.21 The earnings tax exemption provisions are also amended so that SMSFs and small APRA funds are not able to use the segregated assets method in section 295-385 to determine their earnings tax exemption in certain circumstances.

Comparison of key features of new law and current law

New law	*Current law*
Earnings tax exemption provisions	
The earnings tax exemption provisions for complying superannuation funds, RSA providers and life insurance companies in the ITAA 1997 will apply to superannuation income streams that are in the retirement phase at a time. This will cover superannuation income streams that are payable at that time and also deferred superannuation income streams where a person to whom a benefit is payable or will be payable has retired, has a terminal medical condition, is permanently incapacitated or has attained age 65. The earnings tax exemption provisions will not apply to TRISs.	The earnings tax exemption provisions for complying superannuation funds, RSA providers and life insurance companies in the ITAA 1997 apply to superannuation income stream benefits that are payable at a time.

New law	***Current law***
SMSFs and small APRA funds	
SMSFs and small APRA funds will not be able to use the segregated method to determine their earnings tax exemption for an income year if: • at any time during the income year, there is at least one superannuation interest in the fund that is in the retirement phase; and • just before the start of the income year: – a person has a total superannuation balance that exceeds $1.6 million; and – the person is the retirement phase recipient of a superannuation income stream (whether or not the fund is the superannuation income stream provider for the superannuation income stream).	Under Subdivision 295-F, all complying superannuation funds including SMSFs and small APRA funds can use both the segregated and proportional methods to determine their earnings tax exemption on assets that are used to discharge liabilities in respect of current pension liabilities.

Detailed explanation of new law

Background

8.22 Currently, Subdivision 295-F and Division 320 give complying superannuation funds, RSA providers and life insurance companies an earnings tax exemption on income from assets that support currently payable pension and annuity liabilities.

8.23 These provisions are broadly framed in terms of liabilities to provide superannuation income stream benefits (or related concepts) that are currently payable.

8.24 A superannuation income stream benefit is a payment from a superannuation income stream. A superannuation income stream is an income stream that is taken to be an annuity or pension in accordance with the SISR 1994 and RSAR 1997. Annuities and pensions must comply with the minimum standards set out in regulations 1.05 and 1.06 of the SISR 1994 and regulation 1.07 of the RSAR 1997.

8.25 In order to extend the earnings tax exemption to new innovative retirement income products that are deferred superannuation income streams (including guaranteed annuities and group self-annuities), and to remove the earnings tax exemption in respect of TRISs, it is necessary to reframe the earnings tax exemption provisions so that they no longer require superannuation income stream benefits to be currently payable.

8.26 This is because the earnings tax exemption:

- will apply to deferred superannuation income streams prior to superannuation income stream benefits being payable, and
- will no longer be available for TRISs even when superannuation income stream benefits are currently payable.

Retirement phase

8.27 Schedule 8 to the Bill amends the ITAA 1997 so that the earnings tax exemption provisions now apply to complying superannuation funds, RSA providers and life insurance companies if a superannuation income stream is in the 'retirement phase'.

8.28 A superannuation interest will be in the retirement phase at a time if it supports a superannuation income stream that is in the retirement phase at that time. ***[Schedule 8, Part 1, item 29, the definition of 'retirement phase' in subsection 995-1(1)]***

8.29 A superannuation income stream will be in the retirement phase if a superannuation income stream benefit is payable from it at that time. This is the default rule. ***[Schedule 8, Part 1, items 14 and 29, subsection 307-80(1) and the definition of 'retirement phase' in subsection 995-1(1)]***

8.30 A superannuation income stream is also in the retirement phase at a time if it is a deferred superannuation income stream and a superannuation income stream benefit will be payable from it to a person after that time, and the person has retired, has a terminal medical condition, is permanently incapacitated or has attained the age 65. This exception is for deferred superannuation income streams that are not currently payable. Once a deferred superannuation income stream becomes payable it will be covered by the default rule. ***[Schedule 8, Part 1, items 14 and 29, subsection 307-80(2) and the definition of 'deferred superannuation income stream' in subsection 995-1(1)]***

8.31 A deferred superannuation income stream has the meaning given by the SISR 1994. ***[Schedule 8, Part 1, item 29, definition of 'deferred superannuation income stream' in subsection 995-1(1)]***

8.32 Currently, 'deferred superannuation income stream' is not defined in the SISR 1994, however this will be included in the related regulations that will amend the annuity and pension standards in the SISR 1994 to facilitate the development of the new innovative retirement income products.

8.33 A deferred superannuation income stream (which will include guaranteed annuities and group self-annuities) will be a superannuation income stream where the rules governing the income stream meet these new standards.

8.34 If an individual purchases a deferred superannuation income stream prior to meeting one of the relevant nil conditions of release, the earnings tax exemption will not apply until one of the conditions is met. If an individual satisfies a condition of release prior to purchase (e.g. retirement), the earnings tax exemption will apply from the purchase date.

8.35 For example, where an individual purchases a deferred pension from the age of 55 that pays an income stream from the age of 80, the earnings tax exemption will apply from the date the individual satisfies a condition of release such as retirement or attaining the age of 65. Where an individual purchases a deferred pension at the age of 70 that pays an income stream from the age of 80 the earnings tax exemption will apply from the purchase date.

8.36 A superannuation income stream will not be in the retirement phase if it is a TRIS, a TRIP, a non-commutable allocated annuity or a non-commutable allocated pension. ***[Schedule 8, Part 1, item 14, subsection 307-80(3)]***

8.37 A superannuation income stream will also not be in the retirement phase if a superannuation income stream provider has failed to comply with a commutation authority in respect of the transfer balance cap measure. ***[Schedule 8, Part 1, item 14, subsection 307-80(4)]***

Earnings tax exemption provisions for complying superannuation funds

8.38 Complying superannuation funds will receive the earnings tax exemption in respect of retirement phase (RP) superannuation income stream benefits of the fund at the time. ***[Schedule 8, Part 1, items 1 to 3 and 6 to 8, paragraphs 295-385(3)(a) and (4)(a), subsections 295-385(5), 295-390(3) and (7) and 295-395(2)]***

8.39 A superannuation income stream benefit is an RP superannuation income stream benefit of a superannuation fund if it is payable by the fund at that time from a superannuation income stream that is in the retirement phase at that time. ***[Schedule 8, Part 1, items 14 and 29,***

subsection 307-75(1) and the definition of 'retirement phase superannuation income stream benefit (or RP superannuation income stream benefit)' in subsection 995-1(1)]

8.40 A superannuation income stream benefit is also an RP superannuation income stream benefit of a superannuation fund at a time if it is payable by the fund after that time from a superannuation income stream that is a deferred superannuation income stream and is in the retirement phase at that time. ***[Schedule 8, Part 1, items 14 and 29, subsection 307-75(2) and the definition of 'retirement phase superannuation income stream benefit (or RP superannuation income stream benefit)' in subsection 995-1(1)]***

Earnings tax exemption provisions for RSA providers

8.41 RSA providers will receive the earnings tax exemption in respect of a covered superannuation income stream. A superannuation income stream will be covered if it is a pension (within the meaning of the *Retirement Savings Accounts Act 1997*) and it is in the retirement phase. ***[Schedule 8, Part 1, items 10 and 11, sections 295-405 and 295-407, and paragraph 295-410(a)]***

Earnings tax exemption provisions for life insurance companies

8.42 Life insurance companies will receive the earnings tax exemption in respect of either RP superannuation income stream benefits:

- where an exempt life insurance policy is held by a trustee of a complying superannuation fund; and
- in respect of annuities that are superannuation income streams that are in the retirement phase. ***[Schedule 8, Part 1, items 16 to 19, items 21 to 26, paragraphs 320-137(3)(d) and (3)(e), subsection 320-137(3A), paragraph 320-246(1)(a), subparagraphs 320-246(1)(b)(i) and (1)(e)(ii) and paragraphs 320-246(1)(ea), 320-247(1)(a) and 320-247(2)(a)]***

Life insurance companies – transfer of assets

8.43 Life insurance policies that are held to support superannuation income stream benefits paid from a TRIS will no longer be exempt life insurance policies because a superannuation income stream will not be in the retirement phase if it is a TRIS. As such, these policies will be reclassified as complying superannuation life insurance policies.

8.44 As a consequence of this reclassification, a life insurance company may need to transfer assets supporting these policies from its segregated exempt assets to its complying superannuation asset pool. Consequential amendments will allow life insurance companies to transfer assets in these circumstances without triggering unintended tax consequences. ***[Schedule 8, Part 1, items 20, 27 and 28, subsections 320-185(4) and 320-250(1) and paragraph 320-255(1)(a)]***

Superannuation death benefits

8.45 Subregulations 995-1.01(2) to (5) of the *Income Tax Assessment Regulations 1997* (ITAR 1997) expand the meaning of the term 'superannuation income stream benefit' for the purposes of the earnings tax exemption provisions. These subregulations ensure that, where a complying superannuation fund member was receiving a superannuation income stream immediately before their death, the superannuation fund will continue to be entitled to the earnings tax exemption in the period from the member's death until their benefits are cashed by paying them out as a lump sum and/or by commencing a new superannuation income stream.

8.46 These subregulations will continue to work as they currently do despite the earnings tax exemption provisions being reframed in terms of 'RP superannuation income stream benefits'. This is because an RP superannuation income stream benefit is defined in terms of a superannuation income stream benefit.

Excluding SMSFs and small APRA funds with members that have large balances from segregating assets

8.47 If a complying superannuation fund is covered by section 295-387,assets of the fund cannot be segregated for an income year. ***[Schedule 8, Part 1, items 4 and 9, subsections 295-385(7) and 295-395(3)]***

8.48 A complying superannuation fund will be covered by section 295-387 if:

- the fund is either an SMSF as defined by sections 17A and 17B of the *Superannuation Industry (Supervision) Act 1993,* or a fund with less than 5 members (generally known as a small APRA fund) at any time during the income year; and
- at any time during the year there is at least one interest in the fund in the retirement phase; and
- just before the start of the income year:
  - a person has a total superannuation balance that exceeds $1.6 million;
  - the person is a retirement phase recipient of a superannuation income stream; and

– at any time of the year that person has a superannuation interest in the fund. ***[Schedule 8, Part 1, item 5, section 295-387]***

8.49 It will not be necessary for a person with an interest in the small fund to be receiving an income stream from that fund. A small fund will be excluded from using the segregated assets method where a member of the fund, with a total superannuation balance that exceeds $1.6 million, is a retirement phase recipient of an income stream from another superannuation income stream provider. ***[Schedule 8, Part 1, item 5, subsection 295-387(2)(c)]***

Example 8.1: Individual with a large balance

On 30 June 2017 Jeremy has a total superannuation balance of $2.1 million in retirement phase, with a $1.6 million allocated pension in an SMSF and a $500,000 allocated pension with ABC retail superannuation fund. On 1 July 2017 he rolls over $500,000 from his SMSF into a new SMSF as an accumulation interest.

As Jeremy had a total superannuation balance exceeding $1.6 million on 30 June 2017, neither of the SMSFs he is a member of are able to calculate exempt income using the segregated method and must use the proportional method for the 2017-18 financial year. The retail superannuation fund is not affected and can use either method to calculate exempt income

8.50 A total superannuation balance just before the start of an income year will be determined using the method in section 307-230. This will be the sum, at that point in time, of an individual's superannuation interest in the accumulation phase, the balance of any transfer balance account (adjusted to disregard any account based income stream interests), the balance of any account based income stream, and any superannuation roll-over amounts not otherwise reflected in the total superannuation balance. See paragraphs 6.21 to 6.38.

8.51 Assets of funds covered by section 295-387 are known as *disregarded small fund assets*. Such assets cannot be segregated current pension assets for the purposes of section 295-385 or segregated non-current assets for the purposes of section 295-395. ***[Schedule 8, Part 1, items 4, 5, 9 and 29, sections 295-385, 295-387 and 295-395 and the definition of 'disregarded small fund assets' in subsection 995-1(1)]***

8.52 As a result, these funds must calculate their earnings tax exemption for funding current pension liabilities of an income year under section 295-390, applying the proportional method with no assets taken to be segregated to pay current or future liabilities.

Consequential amendments

Proportioning rule

8.53 Section 307-125 of the ITAA 1997 contains the proportioning rule for the taxation of superannuation benefits. Currently, if a superannuation benefit arises from the commutation of a superannuation income stream, the proportioning rule is applied when superannuation income stream benefits commence being made from the income stream.

8.54 The proportioning rule is amended so that if a superannuation income stream benefit arises from the commutation of a deferred superannuation income stream before the commencement day of the income stream, the rule is applied at the time just before the commutation occurred. ***[Schedule 8, Part 1, item 15, paragraph 307-125(3)(c)]***

Tax treatment of a lump sum payment arising from a partial commutation

8.55 Currently, an individual is able to elect under paragraph 995-1.03(b) of the ITAR 1997, before a payment is made, that the payment is not to be treated as a superannuation income stream benefit (making it a superannuation lump sum).

8.56 As discussed at paragraph 8.13, a related regulation will remove this election as one of the measures announced as part of the Government's 2016-17 Budget Superannuation Reform Package.

8.57 This will have an unintended consequence for individuals who partially commute their superannuation income stream. These individuals will no longer be able to make an election that the payment is a superannuation lump sum, which means the payment will be a superannuation income stream benefit.

8.58 However, lump sum payments arising from a partial commutation should be treated for both tax and superannuation purposes as superannuation lump sums. While this is appropriate, it will have the effect of preventing a superannuation fund from claiming the earnings tax exemption under section 295-385 to the extent that assets will no longer be held 'solely' to discharge liabilities in respect of superannuation income stream benefits (as it has supported the payment of a lump sum).

8.59 A consequential amendment is made so that a lump sum payment arising from a partial commutation of a superannuation income stream is generally treated as a superannuation lump sum for the purposes of the ITAA 1997. However, for the purposes of the exempt income provisions in Subdivision 295-F a lump sum payment arising from a partial commutation of a superannuation income stream will be a

superannuation income stream benefit. ***[Schedule 8, Part 1, items 12 and 13, section 307-65]***

Application and transitional provisions

8.60 The amendments in Schedule 8 commence on the first 1 January, 1 April, 1 July or 1 October to occur after the day the amendments receive Royal Assent. ***[Item 2 in the table in section 2 of the Bill]***

8.61 The amendments in Schedule 8 apply for the 2017-18 income year and later income years. ***[Schedule 8, Part 2, item 30]***

Chapter 9
Anti-detriment provisions

Outline of chapter

9.1 For the purpose of consultation, this Chapter of the explanatory material covers proposed amendments in both the exposure draft bill and the exposure draft regulations.

9.2 The exposure draft of Schedule 2 to the Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (the Bill) removes the income tax deduction available to a complying superannuation fund, or approved deposit fund that pays an increased superannuation lump sum, because of the death of a member for the benefit of their spouse, former spouse or child, to compensate for income tax paid by the fund in respect of contributions made for the member during their lifetime.

9.3 The exposure draft of Schedule 2 to the Regulation makes a number of consequential amendments to regulations to reflect the repeal of the deduction.

9.4 All legislative references in this Chapter are to the *Income Tax Assessment Act 1997* unless otherwise specified.

Context of amendments

9.5 The measure forms part of the Government's Superannuation Reform Package announced in the 2016-17 Budget. The measure improves the integrity and fairness of the superannuation system.

9.6 Following the death of a member of a superannuation fund or approved deposit fund, a payment can be made to a beneficiary or to the trustee of a deceased estate. The payment can be made as a superannuation lump sum, or to dependants of the member, as a superannuation income stream.

9.7 Currently the deduction under section 295-485 (the anti-detriment deduction) generally entitles complying superannuation funds and complying approved deposit funds to an income tax deduction when they provide a lump sum benefit because of the death of a member

for the benefit of their spouse, former spouse or children. The amount a fund may deduct is broadly:

- the amount by which the benefit is greater than it would otherwise be to compensate for the income tax that was payable on the member's contributions;
- divided by the income tax rate that applies to assessable contributions to the fund (that is the amount of tax the fund is expected to have borne in relation to the contributions).

9.8 The anti-detriment provision is inconsistently applied by funds. While the concession is intended to benefit certain dependants of deceased members, it relies upon the actions of funds. This is because not all funds are willing or able to increase benefits payable because of death.

9.9 The deduction was originally introduced to smooth the transition when superannuation contributions became subject to income tax in the hands of superannuation funds by ensuring that recipients of benefits paid in respect of a member's death were not disadvantaged. The transitional measures are no longer warranted and are inconsistent. Removing the anti-detriment income tax deduction better aligns the treatment of lump sum benefits paid in respect of the death of members across all complying superannuation and approved deposit funds and the treatment of bequests outside of the superannuation system. The taxation treatment in the hands of recipients of lump sum benefits paid in respect of the death of a member is not changed.

Summary of new law

9.10 The amendments remove the anti-detriment deduction from the income tax law.

Comparison of key features of new law and current law

New law	*Current law*
Anti-detriment deduction	
Complying superannuation funds and complying approved deposit funds are not entitled to claim an income tax deduction if they pay a superannuation benefit on the death of a member to benefit their spouse, former spouse or children and this benefit is greater than it would otherwise be to compensate for income tax paid by the fund in respect of contributions made during the member's lifetime.	Complying superannuation funds and complying approved deposit funds are entitled to claim an income tax deduction if they pay a superannuation benefit on the death of a member to benefit their spouse, former spouse or child and this benefit is greater than it would otherwise be to compensate for income tax paid by the fund in respect of contributions made during the member's lifetime.

Detailed explanation of new law

9.11 The amendments repeal section 295-485 (the anti-detriment deduction). This section allowed complying superannuation and approved deposit funds an income tax deduction if a lump sum superannuation benefit paid to benefit the spouse, former spouse or children of a member following a member's death was greater than it would otherwise have been to compensate for tax payable on the contributions to the fund made for the member over the member's lifetime. ***[Schedule 9, item 3, section 295-485]***

9.12 Removing the anti-detriment income tax deduction better aligns the treatment of lump sum benefits paid in respect of the death of members across all complying superannuation and approved deposit funds and the treatment of bequests outside of the superannuation system. The taxation treatment in the hands of recipients of lump sum benefits paid in respect of the death of a member is not changed.

Example 9.1: No entitlement to deduction

John is a superannuation fund member who passes away in February 2018. John has two children, Miranda and Sam. John's superannuation fund pays Miranda and Sam a superannuation lump sum death benefit. Although Sam and Miranda are John's children, because of these amendments the superannuation fund is not entitled to claim an income tax deduction for any increase in the amount of these payments to compensate for the income tax paid on contributions made in respect of John's superannuation interest with the fund.

Consequential amendments

9.13 Schedule 9 to the Bill and Schedule 2 to the Regulation also make a number of consequential amendments to income tax law (including the transitional provisions) and the *Income Tax Assessment Regulations 1997* to remove items that become redundant following the repeal of the deduction. ***[Schedule 9, items 1, 2, 4, table item headed "superannuation and related business" in the table in section 12-5 and group heading before section 295-485 of the ITAA 1997 and sections 295-485A and 295-485 of the Income Tax (Transitional Provisions) Act 1997 and Schedule 2 to the Regulation, items 1 to 3 and 5 to 6, paragraph 307-125.02(1)(c), paragraph (a) of step 1 of the method statement in subregulation 307-125.02(2), definition of "anti-detriment increase" in subregulation 307-125.02(3) of the Income Tax Assessment Regulations 1997, the definitions of "anti-detriment payment" and "insured benefit" in regulation 4.07C of the Superannuation Industry (Supervision) Regulations 1994]***

Application and transitional provisions

9.14 The amendments in Schedule 9 commence on the start of the first day of the first quarter following Royal Assent. ***[Item 2 of the table in subsection 2(1) of the Bill and table item 1 of the table in section 2 of the Treasury Laws Amendment (Fair and Sustainable Superannuation) Amending Regulation 2016]***

9.15 The repeal applies in relation to superannuation lump sum benefits that are paid because of the death of a member where that member died on or after 1 July 2017. However, from 1 July 2019, it applies to all superannuation lump sum benefits paid after this time, irrespective of whether the member died before 1 July 2017. ***[Schedule 9 of the Bill, item 5 and Schedule 2 of the Treasury Laws Amendment (Fair and Sustainable Superannuation) Amending Regulation 2016, items 4 and 7, regulation 910-1.09 of the Income Tax Assessment Regulations 1997 and regulation 14.13 of the Superannuation Industry (Supervision) Regulations 1994]***

9.16 This ensures that delays in the payment of superannuation benefits in respect of the death of a member in the first two years after the repeal do not result in differences in income tax treatment. However, limiting the transition period to two years avoids uncertainty and compliance costs that would result from indefinitely retaining the income tax deduction in respect of members that pass away prior to 1 July 2017 where payment of benefits to beneficiaries is significantly delayed.

Example 9.2: Entitlement to income tax deduction

Susan is a complying superannuation fund member who passes away on 30 June 2017 and is survived by her husband, William. In December 2017, Susan's superannuation fund pays William a lump sum death benefit, representing the value of Susan's interest and an amount equal to the estimated income tax that has been paid in respect of the superannuation contributions made during Susan's lifetime. The superannuation fund is entitled to claim an income tax deduction under section 295-485 (the anti-detriment deduction) in respect of the payment, as Susan passed away before 1 July 2017.

Example 9.3: No entitlement to income tax deduction

Reuben is a complying superannuation fund member who passes away on 15 July 2017 and is survived by his adult son Alexander. Reuben's superannuation fund pays Alexander a lump sum death benefit. The superannuation fund is not entitled to claim an income tax deduction for any increase in the amount of this payment to compensate for the tax paid in respect of contributions to Reuben's superannuation interest with the fund because Reuben passed away after 30 June 2017.

Example 9.4: No entitlement to income tax deduction for payment made after 1 July 2019

George is a complying superannuation fund member who passes away on 15 June 2017 and is survived by his adult son Tim. George's superannuation fund pays Tim a lump sum death benefit. Due to delays in the grant of probate this payment is not made until 29 August 2019. The superannuation fund is not entitled to claim an income tax deduction because, although George passed away before 30 June 2017, the payment was not made until after 1 July 2019.

Chapter 10
Administration

Outline of chapter

10.1 The exposure draft of Part 1 of Schedule 10 to the Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (the Bill) simplifies the taxation law to assist in streamlining the administration of the Division 293 tax regime.

10.2 The measure reduces compliance costs for superannuation providers and individuals where superannuation benefits become payable from defined benefit interests. The measure removes the requirements in the taxation law relating to superannuation interests for which a Division 293 tax debt account is being kept for:

- superannuation providers to notify the Commissioner of Taxation (Commissioner) of the amount of end benefit caps for their members in some circumstances; and

- individuals to notify the Commissioner in any circumstance when their superannuation benefits from such interests first become payable.

10.3 The exposure draft of Part 2 of Schedule 10 to the Bill clarifies that the Commissioner can provide a single notice that includes two or more separate notices that are required to be provided.

10.4 All legislative references, other than those to Division 293 of the *Income Tax Assessment Act 1997* (Division 293) are to Schedule 1 to the *Taxation Administration Act 1953*.

Context of amendments

10.5 These measures form part of the Government's Superannuation Reform Package announced in the 2016-17 Budget. The measures improve the administration of the superannuation system.

End benefit notifications for Division 293 tax

10.6 Division 133 provides for the deferral of Division 293 tax that is owed on concessional contributions for a defined benefit interest. Division 133 also provides that on payment of an end benefit from the defined benefit interest, a superannuation provider must report the end benefit cap for the defined benefit interest to the Commissioner.

10.7 The end benefit cap is 15 per cent of the employer-financed component of any part of the value of the superannuation interest that accrued after 1 July 2012. It ensures that a defined benefit member's deferred Division 293 tax debt reflects the member's defined benefit entitlement.

10.8 In particular, it protects defined benefit members from an unfair tax burden when the value of their defined benefit on exit is significantly lower than would be expected for the level of contributions that have been paid to finance the benefit — for example, when an entitlement is taken early from a scheme that does not vest its benefits evenly each year.

10.9 A superannuation provider of a defined benefit interest is required to advise the Commissioner of the amount of an end benefit cap for a member in certain situations where superannuation benefits first become payable.

10.10 Superannuation providers of defined benefit interests incur significant costs in working out the amount of their members' end benefit cap as it requires an actuarial calculation.

10.11 Prior to these amendments, superannuation providers were required to advise the Commissioner of a member's end benefit cap amount if:

- the Commissioner had started keeping a Division 293 tax debt account for the superannuation interest for the member;
- the Commissioner had given notice to the superannuation provider that a Division 293 tax debt account was being kept for that member; and
- an end benefit became payable from that superannuation interest for that member.

10.12 In addition, prior to these amendments, there was also a requirement for an individual to provide the Commissioner with an individual end benefit notice if they requested a superannuation provider pay an end benefit from a superannuation interest for which the Commissioner had started keeping a Division 293 tax debt account.

Combining notices

10.13 There are a range of circumstances in which the Commissioner has an obligation or may issue a notice to a taxpayer. This includes notices of assessment, determinations, statements and other documents. For the purposes of the combined notices measure, they are collectively referred to as 'notices'.

10.14 There is uncertainty whether the Commissioner can provide multiple notices and other documents such as determinations in a single notice, in the absence of this being expressly authorised by the taxation law. Some parts of the taxation law specifically allow combined notices, whilst other provisions do not expressly deal with this issue.

10.15 In the superannuation context, this inconsistency also exists. For example subsection 292-230(3) of the *Income Tax Assessment Act 1997* (ITAA 1997) contains a specific provision for excess non-concessional contributions tax assessment notices to be contained in one document with other notices, whilst the Division 293 tax assessment provisions in Subdivision 155-A of the *Taxation Administration Act 1953* (TAA) do not.

10.16 Changes to the contribution caps (annual concessional cap and annual non-concessional cap) and to the Division 293 tax income threshold announced as part of the 2016-17 Budget may result in an increase in the number of individuals who receive an assessment from the Commissioner for additional tax under these regimes.

10.17 Sending out separate notices for different superannuation tax regimes (for example Division 293 tax, excess non-concessional contributions tax and excess concessional contributions) does not provide a complete position for taxpayers and creates inefficiencies for the Commissioner.

Summary of new law

End benefit notifications for Division 293 tax

10.18 The measure reduces compliance costs for superannuation providers and individuals where superannuation benefits become payable for defined benefit interests.

10.19 The measure removes the compliance requirements under Division 293 for superannuation providers to notify the Commissioner of the amount of end benefit caps in some circumstances. Notification is not required if the superannuation provider's member does not have a Division 293 tax debt account amount owing at the time the member's superannuation benefit first becomes payable.

10.20 The measure also reduces superannuation compliance costs for individuals with defined benefit superannuation interests by removing the requirement for them to notify the Commissioner when their superannuation benefits for such interests first become payable.

Combining notices

10.21 This measure clarifies that the Commissioner can provide a single notice that includes two or more separate notices that are required to be provided under the taxation law.

Comparison of key features of new law and current law

New law	*Current law*
Superannuation provider's notification of end benefit cap amount	
The amendments do not require a superannuation provider of a defined benefit interest to disclose the amount of their member's end benefit cap when they give the Commissioner an end benefit notice if the provider has confirmed with the Commissioner that there is no amount owing on the member's Division 293 tax debt account.	A superannuation provider of defined benefit interests is required to give the Commissioner an end benefit notice disclosing their member's end benefit cap amount once the end benefit has become payable from the interest if the Commissioner has: • started keeping a Division 293 tax debt account for the superannuation interest; and • given notice to the superannuation provider that a Division 293 tax debt account is being kept.

New law	*Current law*
Individuals not required to provide end benefit notices	
There is no longer a requirement for an individual to provide the Commissioner with an individual end benefit notice.	An individual must notify the Commissioner by providing an individual end benefit notice if the individual requests a superannuation provider pay an end benefit from a superannuation interest and the Commissioner has established a Division 293 tax debt account in relation to that interest.
Combining notices	
The amendments clarify and confirm that the Commissioner can provide a single notice to a taxpayer which contains two or more separate notices for that taxpayer that are required to be given under any taxation law.	The taxation law in some cases specifically provides that the Commissioner may include a notice to a taxpayer with another notice to that taxpayer. In some cases that other notice has to be issued under the same Act as the notice that is to be issued. In other cases, there is no provision that specifically authorises a notice to be given with another notice.

Detailed explanation of new law

Superannuation provider's notification of end benefit cap amount

10.22 Part 1 of Schedule 10 to the Bill removes the need for a superannuation provider of defined benefit interests to advise the Commissioner of an end benefit cap amount if the superannuation provider has confirmed with the Commissioner that their member does not have an amount owing on the member's Division 293 tax debt account. ***[Schedule 10, Part 1, item 8, subsection 133-140(1A)]***

10.23 Following receipt of a member's request to pay an end benefit from a defined benefit superannuation interest the superannuation provider may, if it opts to do so, request that the Commissioner confirm if there is an amount owing on the Division 293 tax debt account that is associated with the interest. The Commissioner will be required to confirm this within a reasonable time. ***[Schedule 10, Part 1, item 6, section 133-135]***

10.24 The superannuation provider will not need to include the amount of the end benefit cap in their end benefit notification if the

superannuation provider obtains the Commissioner's confirmation that there is no amount owing on the Division 293 tax debt account. The Commissioner will develop administrative processes to provide superannuation providers with evidence of such confirmation. ***[Schedule 10, Part 1, items 6 and 8, subsections 133-135(2) and 133-140(1A)]***

10.25 Alternatively, the superannuation provider could choose not to request the above information from the Commissioner and provide an end benefit notification which includes the amount of the end benefit cap amount. Given the costs of calculating the end benefit cap amount it is expected that most superannuation providers will seek information from the Commissioner about the status of their members' Division 293 tax debt accounts.

10.26 However, the superannuation provider will still have to provide an end benefit notice as required under the existing law even if the end benefit cap amount does not have to be provided (see section 133-140). This is because the Commissioner continues to need notification of the pending payment of the superannuation benefit to close the Division 293 tax debt account in relation to the superannuation interest and to seek payment of any future Division 293 amounts payable.

Example 10.1: Superannuation provider not required to advise of end benefit cap amount

Sophie is planning to retire and has requested her superannuation provider pay her an end benefit from her defined benefit superannuation interest. Following receipt of her request, Sophie's superannuation provider contacts the Commissioner about the status of her Division 293 tax debt account. The Commissioner confirms there is no amount owing on the account.

Sophie's superannuation provider will not be required to report an end benefit cap amount. However, the provider will still need to give the Commissioner an end benefit notification for her superannuation interest. This allows the Commissioner to close Sophie's Division 293 tax debt account.

10.27 In addition to making consequential changes, the amendments also simplify the existing subsection 133-120(1) by splitting it into two provisions to make it easier to apply. This is not intended to change the application of the subsection in any way. ***[Schedule 10, Part 1, item 2, subsections 133-120(1) and (1A)]***

Individuals not required to provide end benefit notices

10.28 Part 1 of Schedule 10 to the Bill also removes the need for individuals with defined benefit superannuation interests to provide the

Commissioner with an individual end benefit notice. Previously this notice was required by individuals who requested that their superannuation provider pay an end benefit from their superannuation interest for which the Commissioner kept a Division 293 tax debt account.

10.29 This amendment removes this compliance obligation on individuals, and recognises that the Commissioner will continue to receive end benefit notifications from superannuation providers which provide the Commissioner with the information the Commissioner requires.

Example 10.2: Individual end benefit notification not required

Peter is retiring and requests his superannuation provider pay him an end benefit from his defined benefit superannuation interest for which the Commissioner has been keeping a Division 293 tax debt account. There is no need for Peter to give the Commissioner an individual end benefit notice to advise the Commissioner of the request.

Combining notices

10.30 Part 2 of Schedule 10 to the Bill introduces a specific provision to clarify and remove any doubt that the Commissioner can provide a single notice that includes two or more separate notices required to be provided under a taxation law. ***[Schedule 10, Part 2, item 11, section 990-5 in Schedule 1 to the TAA]***

10.31 An approach under which the Commissioner combines multiple notices into one document reduces compliance costs for taxpayers. For example, providing one notice that contains assessment notices for Division 293 tax and excess non-concessional contributions tax and notices concerning excess concessional contributions ensures affected taxpayers receive a more comprehensive picture of their superannuation tax position and allows them to seek advice about all matters at the one time rather than at different times.

10.32 The benefits from the Commissioner being able to include multiple notifications and determinations in a single notice apply wider than just superannuation. Accordingly, this measure applies to all taxes, not just aspects of the taxation law that concern superannuation.

10.33 The Commissioner can decide if notices should be combined. In doing so, the Commissioner would take into account existing administrative practice regarding the affected notices and the benefits to taxpayers from consolidating them.

Consequential amendments

10.34 Part 1 of Schedule 10 to the Bill also makes several consequential amendments to the *Taxation Administration Act 1953* to facilitate the changes to Division 293 tax end benefit notification. ***[Schedule 10, Part 1, items 1, 3 to 5 and 9, subsection 133-10(3), section 133-125 and subsection 133-145(1)]***

10.35 Part 2 of Schedule 10 to the Bill also makes consequential amendments to the taxation law to remove provisions allowing the Commissioner to include a notice with any other notice that the Commissioner provides to a taxpayer. These provisions will be redundant following the enactment of the new provision to combine notices contained in Part 2 of this Schedule. ***[Schedule 10, Part 2, items 12 to 38, subsections 45D(1), 102AAM(13), 159GZZZZH(3), 177EA(6), 177EB(7) and 177F(2D) of the Income Tax Assessment Act 1936, subsections 204-50(4), 214-60(3), 214-140(1), 214-140(2), 275-615(3), 291-465(6), 292-230(3), 292-310(3), 292-465(8), 292-467(3), 295-625(1), 295-625(2), 815-30(8), 815-35(8) and 815-145(6) of the ITAA 1997, subsections 214-25(3), 214-80(1) and 214-80(2) of the Income Tax (Transitional Provisions) Act 1997, subsection 98C(2) of the Petroleum Resource Rent Tax Act 1987, subsection 62(2) of the Superannuation Guarantee (Administration) Act 1992, subsection 8AAF(3) of the TAA and subsections 45-320(6), 45-473(1), 45-473(2), 97-5(4), 97-25(4), 133-30(2) and 280-110(2) in Schedule 1 to the TAA]***

Application and transitional provisions

10.36 The amendments in Schedule 10 commence on the first day of the next quarter following the day of Royal Assent.

10.37 The amendments in Part 1 of Schedule 10 apply to end benefit notifications for which the obligation to provide the notification arises on or after 1 July 2017. ***[Schedule 10, Part 1, item 10]***

10.38 The amendments in Part 2 of Schedule 10 apply on and from 1 July 2017. ***[Schedule 10, Part 2, item 39]***