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TAX ALERT: NEW SUPERANNUATION CONTRIBUTION CAPS

Introduction

Following the 2016 Federal Budget announcement on 3 May 2016, there has been a significant amount of commentary, concern and confusion surrounding some of the changes announced, in particular the new lifetime non-concessional contribution cap for superannuation.

Firstly, it is difficult to know exactly how final the announced changes are, when a budget is handed down by a Government that will not have enough time to pass any measures before it goes into an election. Do we follow the current laws or the laws as they are proposed to be changed in the future (if the Government is re-elected and if it can pass the measures in the newly constituted parliament)?

Although that is the situation we find ourselves in with the announced super changes, we should adopt the most conservative approach and prepare for these new rules in relation to the lifetime non-concessional contributions cap to apply from Budget Night (ie. at 7.30pm on 3 May 2016).

Lifetime cap on non-concessional contributions

The proposed lifetime cap of $500K (indexed) will replace the annual non-concessional contribution cap (currently $180K or $540K for 3 years under the bring-forward rule). The cap will be measured retrospectively to contributions made from 1 July 2007.

Contributions made from 1 July 2007 will be counted against the $500K lifetime limit. If you have exceeded the $500K cap at Budget night, (ie. at 7.30pm on 3 May 2016), you will not be required to remove the excess and no penalty will apply.

Any after tax contributions made after 7.30pm on 3 May 2016 that exceed the $500K limit will need to be removed or a penalty tax will apply.

The obvious risks associated with this announcement

The potential for error here is considerable when all non-concessional contributions over nine years need to be identified. While this may be a difficult enough task to confirm nine years of records for one super fund, it becomes exponentially complex where a member may have multiple super funds, including retail and industry funds, some of which may have merged etc. since 2007.

Add to this the need to review previously acceptable strategies such as a “re-contribution strategy”, where certain members took annual pensions and simply re-contributed the payments as non-concessional contributions every year.

The unexpected risks associated with this announcement

This announcement may impact on limited recourse borrowing arrangements (LRBA) which have been in place for some time.

For example, in circumstances where a member has a LRBA secured over a commercial property investment. In the past if the super fund lost a tenant for a period of time, a member could make non-concessional contributions to the super fund to cover the interest payments on the LRBA.

Today, if the member has maxed out the lifetime cap of $500K in non-concessional contributions since 1 July 2007, and the same circumstances were to occur by losing a tenant, the member would not be able to make additional non-concessional contributions to solve their LRBA problem without exceeding the lifetime limit and being penalised for excess contributions.

Furthermore, some super funds may rely on members contributing to their fund to assist in repaying borrowings undertaken through a LRBA. If members have already used their lifetime non-concessional contributions cap, it may be difficult for some super funds to obtain sufficient cash flow to meet their borrowing commitments.

Some super funds may need to change a LRBA so that it is on terms that meet the loan to value ratio (LVR) requirements in the safe harbour rules (ie. must not exceed 70% for real property or 50% for listed shares or units); however many funds may simply not have sufficient access to cash to pay down their loans adequately.

The retrospective application of the lifetime non-concessional contributions cap may prevent super funds from being able to pay down their loans to fall within the LVR safe harbours by 30 June 2016.

Conclusion

The new lifetime non-concessional contributions cap of $500K applies from 7.30pm on 3 May 2016, and a nine year review of past non-concessional contributions needs to be performed to ensure a member complies with the announcement going forward.

Clearly this places an onerous administrative obligation and potentially costly exercise for most super fund members.

We recommend to all members that they immediately consider the potential impacts of these rules, as detailed above; as we should treat the announcement as if it were law today. If members have any concerns to contact their Lowe Lippmann Relationship Partner.

Please do not hesitate to contact your Lowe Lippmann Relationship Partner if you wish to discuss any of these matters further.