Super Tax News

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Earnings from super balances above $3m to be taxed at an additional 15% from 2025-26

KEY COMMENTS

In the Budget, the Treasurer confirmed the previous Government announcement that individuals with superannuation balances above $3 million will be taxed at an additional 15 per cent on the earnings (as opposed to the taxable income) that relate to the excess.

This additional tax is levied at the individual member level and not the fund level.

Taxable income at the fund level will still be subject to tax in the fund at the normal rates of either 15 or 0 per cent.

Importantly, as taxable income cannot be calculated at an individual member level (particularly for large funds) the proposal uses earnings as a proxy.

Two consequences of this are that, firstly, the additional tax is payable an increase in earnings attributable to both realised and unrealised gains and secondly, the benefit of the CGT discount is lost.

In the Budget, the Treasurer confirmed the previous Government announcement that individuals with superannuation balances over $3 million will be taxed at an additional 15 per cent on the earnings that relate to that excess.

Currently, the concessional tax rate on superannuation earnings is up to 15 per cent (in relation to assets in accumulation phase) or 0 per cent (in relation to assets in pension phase).

The announced change is proposed to come into effect on 1 July 2025 and apply from 2025-26.

According to Budget Paper No.2, the additional tax on earnings imposed by this measure will impact around 80,000 individuals in 2025-26, or approximately 0.5 per cent of individuals with a superannuation account. In 2027-28, the first full year of receipts collection, the measure is expected to increase receipts by $2.3 billion.

Only earnings in relation to the part of the balance in excess of $3 million are subject to the additional tax. The $3 million threshold is a 'hard' number and is currently not subject to indexation unlike other thresholds (for example, the transfer balance cap). This means that in the future, unless the threshold is indexed, that over time this measure will capture a greater share of members.

The additional tax is levied at the member level and not the fund level. Taxable income will still be subject to tax in the fund at the normal rates of either 15 or 0 per cent. Accordingly, there is no change to fund level taxation. Importantly, there is no credit for any additional tax paid by the member for any fund level taxation. That is, the two regimes operate independently of each other.

In addition, negative earnings (i.e. losses) will be able to be carried forward and used to offset against future years' tax liabilities.

Individuals who are affected by this measure can elect either to pay the additional liability themselves or to direct the superannuation fund to release funds to fund this liability.

It is interesting to note that there is no limit placed on the size of superannuation account balances in the accumulation phase. Interestingly, where a member has a total superannuation balance in excess of the $3 million, there is no requirement to withdraw this excess from the system.

In addition, it is expected that the effective tax rate for affected members may be higher than the actual 15% due to the tax being levied on earnings which includes taxing unrealised gains without the benefit of the CGT discount.

The Government claims this change is consistent and aligned with the Government's proposed objective of superannuation to deliver income for a dignified retirement in an equitable and sustainable way.

There will be further consultation undertaken with relevant stakeholders, both within and outside of the superannuation industry. As this measure is not expected to apply until at least the year commencing 1 July 2025, and as there will be another Federal Election prior to this, much may change during this interval.

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Non-arm's length income ("NALI") / non-arm's length expenditure ("NALE")

KEY COMMENTS

The Treasurer announced in the Budget that the Government would amend the non-arm's length income ("NALI") provisions, in relation to expenditure incurred by superannuation funds, by exempting large APRA-regulated funds from the NALI provisions for both general and specific expenses of the fund. The NALI provisions with respect to income will still operate as normal.

Previously, Treasury had announced a proposal to exempt large APRA-regulated funds from the NALI provisions with respect to general expenses only. This measure now extends this proposal to both general and specific expenses.

In short, this change takes funds back to the NALI rules as they applied prior to the changes to include NALE. That is, funds still need to consider whether income they receive could be considered to be non-arm's length (e.g. a private company dividend).

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Previously, Treasury had announced a proposal to exempt large APRA-regulated funds from the NALI provisions with respect to general expenses only. This measure now extends this proposal to both general and specific expenses.

What does this mean for large funds?

In short, this change takes funds back to the NALI rules as they applied prior to the changes to include NALE. That is, funds still need to consider whether income they receive could be considered to be non-arm's length (e.g. a private company dividend).

This outcome is appropriate, as we maintained there was no mischief present that required a NALE rule for large funds.

Now, funds can incur expenditure from a related party (e.g. a service provider, a wholly-owned company etc.), without having to worry that the ATO might at a later stage determine that the expenditure was non-arm's length and thereby treat some or all of the fund's income as non-arm's length income and thereby lose the concessional rates of tax – 15% and 0% on that income.

Further, funds will not have to incur significant compliance costs in justifying the arm's length nature of various expenditures incurred with related parties. This is a welcome compliance cost saving.

Of course, when a superannuation fund incurs expenses, it will still need to determine whether the loss or outgoing is:

— Immediately deductible, either under ordinary provisions or a specific provision,

— Deductible, but over a period,

— Included in the cost base of an asset,

— Capital in nature, but deductible over five years under the black hole provisions; or

— Capital in nature and none of the above.

The announcement follows months of ongoing consultation by Government with industry on the application of the NALE rules to large APRA-regulated funds. These changes have been welcomed by industry.

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OTHER FEDERAL BUDGET ANNOUNCEMENTS

Increasing the payment frequency of Superannuation Guarantee

In the Budget, the Treasurer confirmed that the Government intends to amend the superannuation guarantee ("SG") provisions to ensure that, from 1 July 2026, employers will be required to pay their employees' SG entitlements on the same day that they pay salary and wages.

The intention of the change is to ensure that, by increasing the frequency of SG payments from the currently quarterly basis, employees have greater visibility over whether their SG entitlements have been met. Further, it is expected that increased frequency of SG payments by employers should improve retirement outcomes for superannuation fund members.

The proposed start date of 1 July 2016 is designed to ensure that employers, payroll service providers, the ATO and superannuation funds have sufficient time to implement this administrative and systems change.

The Government intends to conduct a consultation process with relevant stakeholders on the details of the proposed change.

Proposed changes to the General Anti-avoidance provisions

In an interesting development, the Government has announced its intention to expand the scope of the general anti-avoidance provisions in Part IVA of the *Income Tax Assessment Act 1936* (Cth) to apply to schemes that:

— reduce tax paid in Australia by accessing a lower withholding tax rate on income paid to foreign residents; or

— achieve an Australian income tax benefit, even where the dominant purpose was to reduce foreign income tax.

This measure will apply to income years commencing on or after 1 July 2024, regardless of whether the scheme was entered into before that date.

It is currently not clear from the available information what is the specific mischief that Treasury is concerned about that warranted the proposed extension of these rules. It will be important to monitor these developments as further details come to light.

'Build to rent' tax incentives

The Government has announced its intention to encourage 'build to rent' housing developments by a combination of accelerated tax deductions and a reduced managed investment trust ("MIT") withholding tax rate applicable to these developments.

The measure will apply to 'build to rent' projects consisting of 50 or more apartments or dwellings made available for rent to the general public. The dwellings must be retained under single ownership for at least 10 years before being able to be sold and landlords must offer a lease term of at least 3 years for each dwelling.

Tax depreciation

The Government will increase the rate for capital works tax deductions to 4% per annum for eligible new 'build to rent' projects where construction commences after 7:30pm AEST on 9 May 2023.

Reduced MIT withholding tax rate

The Government will reduce the final withholding tax rate on eligible fund payments from MIT investments from 30% to 15%. It is understood that the reduced MIT withholding tax rate will apply in respect of relevant projects from 1 July 2024. The expectation is that this measure may increase the attractiveness of these investments for foreign capital.

Importantly, it appears that 'build to rent' projects that commenced prior to Budget night are not eligible for these newly-announced tax incentives.

Additional ATO compliance resources

The Government has allocated increased funding in the Budget for compliance activities undertaken by the ATO.

In particular, there is increased funding for:

— SG compliance;

— the Personal Income Tax Compliance Program; and

— GST compliance.

The additional funding provided will also enable the ATO to better engage with taxpayers who have high-value debts over $100,000 and aged debts older than two years.

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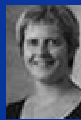

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