INSIDE

MAY 2021

FINANCIAL MATTERS AFFECTING YOUR LIFESTYLE

- Managing your superannuation transfer balance account
- Insurance companies are changing the rules
- When it comes to real estate & CGT look at the timing

Managing your superannuation transfer balance account

Most people think of retirement as a time to put your feet up and relax, but it can also be a time when pre-retirees alike actually need to flex the grey matter.

With all the rules and regulations swirling around the superannuation sector these days, it's not unusual for those nearing retirement to feel compelled to dust off the calculator and bone up on certain superannuation concepts. The transfer balance account and the transfer balance cap are topics that can challenge many retirees.

Transfers into and out of retirement phase are referred to as credit or debit events. Your transfer balance account is calculated by keeping track of these events and is used to determine if you have exceeded your personal transfer balance cap (TBC, more on this below).

All of your retirement phase income streams are taken into consideration, including capped defined benefit income streams and market pensions.

The value of your superannuation interests is calculated by your superannuation fund and reported to the ATO (and if you believe the value reported is incorrect, it is best to contact your super fund or the ATO directly).

CREDITS TO YOUR ACCOUNT

Generally, a credit arises in your transfer balance account when you become the recipient of a superannuation income stream that is in retirement phase.

The following events will cause a credit to your transfer balance account:

- Superannuation income streams that were in existence just before 1 July 2017 and you continue to receive them after that date – including both reversionary and non-reversionary death benefit income streams.
- New superannuation income streams that commenced after 1 July 2017- including both reversionary and non-reversionary death benefit income streams.
- When a transition to retirement income stream starts to be in retirement phase.
- Repayments from limited recourse borrowing arrangements.
- Excess transfer balance earnings.

These credits increase your transfer balance account and reduce your available personal TBC space.

SUPERANNUATION INCOME STREAMS

An income stream is a series of periodic benefit payments to a member. This includes both reversionary and non-reversionary death benefit income streams and can be either:

- Account-based income streams (the amount supporting the income stream is allocated to a member's account), or
- Non-account-based income streams, including capped defined benefit income streams (these are income streams that don't have an identifiable account balance in the members name – the member receives regular payments, usually guaranteed for for life).

ACCOUNT-BASED INCOME STREAM

If you were receiving an account-based superannuation income stream just before 1 July 2017, and you continued to receive it after that date, your fund will have reported the value of all the superannuation interests that support the income stream in retirement phase that you were receiving at that time.

If you started an income stream after 1 July 2017, your fund will report the commencement value of that superannuation income stream. This includes death benefit incomes streams and market linked pensions.

CAPED DEFINED BENEFIT INCOME STREAMS

Capped defined benefit income streams are treated differently because you usually can't commute these income streams, except in limited circumstances.

Capped defined benefit income streams are:

- Lifetime pensions, regardless of when they commence
- Lifetime annuities that existed just before 1 July 2017
- Life expectancy pensions and annuities that existed just before 1 July 2017
- Market-lined pensions and annuities that existed just before 1 July 2017.

The modified value of a capped defined benefit income stream is referred to as the "special value", and this value will be calculated by your superannuation provider.

TRANSFER BALANCE CAP

The transfer balance cap (TBC) is a limit on how much superannuation can be transferred from your accumulation superannuation account to a tax-free retirement phase account. At present, the general TBC is currently $1.6million and all individuals have a personal TBC of $1.6 million.

If you exceed your personal TBC, you may have to:

- Commute (that is, convert a portion of your retirement phase income stream into a lump sum) the excess from one or more retirement phase income strains
- Pay tax on the notional earnings related to that excess.

If the amount in your retirement phase account grows over time (through investment earnings) to more than your personal TBC, you won't exceed your cap. Source: Butler Settineri

INSURANCE COMPANIES ARE CHANGING THE RULES

Changes to income protection insurance:

From 1 July 2021, insurers will have rules in place to make sure benefits do not exceed 100% of your earnings, cease offering guaranteed renewable policies, and have stricter disability definitions for longer benefit periods. On 31 March 2020, new applications for Agreed Value income protection insurance were discontinued, which is particularly worrisome for self-employed people who have fluctuating incomes.

How will it affect you?

New income protection clients buying an income protection policy after 31 March 2020 will have their monthly benefit based on their income at claim time. New clients will not be eligible for Agreed Value policies that provided more certainty at claim time as benefits were determined during the application stage when financials were provided.

Existing Agreed Value income protection client's policy terms and conditions will generally not change; however, your premiums might change in the future.

When will the changes come into effect?

Agreed Value income protection insurance are no longer available from 31 March 2020, with some insurers already notifying brokers and advisers.

Life insurance companies might start implementing other changes earlier. **However, the next planned date for additional changes is set for no later than 1 July 2021.**

APRA has requested that Life Insurance companies provide data regarding the changes implemented by mid-next year so that they can monitor the expected results.

Income protection changes explained:

The end of Agreed Valued polices
Agreed Value and Endorsed Agreed income protection insurance, that locked-in your monthly insurance benefit at application time, will no longer be available to new applications from 31 March 2020.

Agreed Value will be replaced by **Indemnity income protection,** which calculates your benefits on annual earnings at claim time and can thus be affected by any subsequent reductions in your income.

Benefits will be based on your annual earnings of the last 12 months:
From 1 July 2021, your monthly benefit pay-out will be calculated on what you earned during the 12 consecutive months before you got sick or injured. Previously, select insurers provided you with the option of reviewing your income over the previous 2 to 3 years and then using the best 12 consecutive months of that period.

Income protection contracts may not exceed 5 years:
Another income protection change to come into effect no later than 1 July 2021, is that yearly guaranteed renewable will be replaced with contracts that cannot be guaranteed renewable for greater than 5 years.

While it proposes that the policy owner can elect to renew their contract for further periods (not exceeding 5 years) without having to undergo a medical review, the renewal will be subject to an analysis of changes in your occupation and financial circumstances.

Limits on income protection payments for the first 6 months:
From 1 July 2021 insurers must ensure your benefit does not exceed 100% of your earnings at claim time for the first 6 months. Life insurance companies will consider your benefit payment and any alternative sources of income you might be receiving.

After 6 months your maximum income protection benefit will be limited to 75% of your earnings at the time of claim, up to $30,000 per month.

Reducing the risk of longer benefit periods:

To encourage clients to recover and return to work sooner, insurers should have controls in place, by 1 July 2021, to reduce the risk of long-term benefit periods. This means stricter disability definitions and setting internal benchmarks for new income protection products with long benefit periods.

Life insurance companies to provide quality data:

From 1 July 2021 APRA expects life insurance companies to deliver up-to-date data promptly, so results of customers experience can be released every 18 months. Source: Life insurance direct Russell Cain

When it comes to real estate and CGT, look at timing

When you sell or otherwise dispose of real estate, the time of the event (when you make a capital gain or loss) is usually when one of the following occurs:

- You enter into the contract (the date on the contract), not when you settle. The fact that a contract is subject to a condition, such as finance approval, generally doesn't affect this date.
- The change of ownership occurs if there is no contract – such as when a property passes to a beneficiary.
- The real estate is compulsorily acquired – the time of the event is earliest of
  - When you receive compensation from the acquiring entity
  - When the entity became the property's owner
  - When the entity enters the property under a power of compulsory acquisition or takes possession under that power.

Although you report your capital gain or loss in the tax return for the income year in which the contract is entered into, you're not required to do this until settlement occurs. If settlement occurs after you've lodged your tax return and been assessed for the relevant income year, you will most likely need to request an amendment.

You may be liable for shortfall interest charge (SIC) because of an amended assessment for a capital gain. The ATO generally remits the SIC in full if the request for amendment is lodged within a reasonable time after the settlement (generally considered to be one month in most cases).

However, remission is not automatic – you must request it in writing, which an accountant can help you with. The ATO says it considers each request on a case-by-case basis, so informed wording of that request can make a difference.

If you consider that the shortfall interest charge should be remitted, it is generally best to provide your reasons when requesting an amendment to your assessment.

Two "main residences" is possible

It is generally accepted that an exemption to capital gains tax applies to the family home, or "main residence", and the exemption usually applies for only one home at any given time. But there is a rule that allows for a taxpayer to have two main residences and still maintain that CGT- free status for both premises for a temporary period.

Known as the "six-month rule", this states that two properties can be claimed as a main residence at the same time where a taxpayer acquires a dwelling that becomes their new main residence before they dispose of the original. This is a sensible allowance for an overlap of periods in which a taxpayer can claim exemption from CGT for two properties – one newly acquired and one that is to be sold. Selling the old house may take longer than six months, but the CGT exemption only holds for that long, and the ATO cannot extend this concession.

It is available for the earlier of; six months after taking ownership of the new house, or when you transfer ownership of the old house. However, there are two prerequisites to qualify – the old house must have been your main residence for at least a continuous three months in the 12 months before transfer; and if it was not your main residence for any of that time it can't have been used to produce income. Source : Butler Settineri

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