

Retirement Income – Transfer balance cap

The transfer balance cap limits the amount that can be transferred into what is known as the 'retirement pension phase' of superannuation and receive the benefit of 0% earnings tax.

Benefits

- Earnings on account based income streams are taxed at 0% if within your transfer balance cap.
- Certain non-account based income streams payments, such as defined benefit pensions, receive favourable tax when assessed within the cap.
- Superannuation savings above the transfer balance cap can continue to be held in the accumulation phase where earnings are taxed at up to 15% which may be lower than your marginal tax rate.
- As the cap applies to each individual, it would allow a couple to have up to \$3.2 million in the 0% earnings environment of superannuation.

How it works

The transfer balance cap limits the amount that can be transferred into what is known as the 'retirement pension phase' of superannuation and receive the benefit of 0% earnings tax.

All individuals have their own transfer balance cap. Your personal cap is determined based on a number of things, including:

- the general transfer balance cap at the time you first commence a retirement phase superannuation income stream,
- any indexation that may be applied to the general transfer balance cap, and
- the total of amounts that you have used to commence retirement phase income streams.

When a superannuation income stream is commenced or transfers to retirement phase, you will start to have what is known as a 'transfer balance account'. This is a notional account, where certain types of transactions you make in relation to your superannuation income streams are recorded. Your transfer balance account relative to the available cap is what determines whether you're eligible to transfer additional amounts to retirement phase pensions in the future.

If your transfer balance account exceeds the cap at any time, additional tax and penalties may apply.

Income streams measured against the transfer balance cap include:

- account based pensions,
- defined benefit pensions, or
- deferred income stream payable or transition to retirement income streams payable to a person who has met one of the following conditions of release:
 - retirement,
 - terminal illness,
 - permanent incapacity, or

Important: This document contains general information about the benefits, costs and risks associated with certain product classes and strategies. It has been prepared without taking into account your objectives, financial situation or needs. Because of this you should, before acting on any advice in this document, consider whether it is appropriate to your personal circumstances.

- reaching age 65.

Death benefit superannuation income streams (with modifications for child death benefit pension) are also treated as retirement phase pensions and are assessed against the cap.

NOTE: Transition to retirement income streams are not assessed against the transfer balance cap until certain conditions of release have been satisfied (see above). Please refer to the 'Transition to Retirement' Understanding Series for further information.

What counts towards your cap?

The transfer balance account operates via a credits and debits system, and doesn't reflect your pension account balances at a particular time. This means that your actual retirement phase pension balance may be more or less than the deemed balance of your transfer balance account.

A credit is an assessment against the cap which will most commonly apply when an income stream commences, or when a person has certain other types of superannuation income streams, such as 'transition to retirement' income stream, and they either reach age 65 or notify their fund that they have met another condition of release.

Where you commence a new account based retirement phase pension, the account balance at commencement is the amount that will be credited to your transfer balance account and assessed against the cap.

A debit arises to reduce the amount assessed against your cap. Debits include adjustments for certain amounts such as:

- contributions made under a structured settlement
- commutations (or lump sums) taken from your income stream, and
- adjustments to meet family law settlements.

Regular pension payments and market movement which may arise due to fluctuations in investment values, do not impact your transfer balance account. That is, they will not result in a credit or a debit.

Certain income streams, including defined benefit pensions, that do not ordinarily have an account balance, have a value determined for the purpose of the transfer balance cap, based on a formula contained in the legislation. The calculation is:

$\text{Annual Income} \times 16$

As you will have your own transfer balance cap and account, the cap therefore includes all superannuation income streams that are payable to you.

Exceeding the cap

An excess transfer balance occurs if the total value of all credits to your transfer balance account exceeds your transfer balance cap. This would exist for example, if the cap was \$1.6 million and you commenced a pension with \$1.8 million. In this case, you would receive a credit for \$1.8 million, and would have a \$200,000 excess transfer balance amount.

You would not be deemed to have an excess however, if your cap was \$1.6 million, you commenced a pension with this amount, and through investment returns, your account balance increased to \$1.8 million over time. This is because you would only receive a credit to your transfer balance account of \$1.6 million, as this is the amount you used to commence your pension, and market movement doesn't result in a debit or a credit.

In the case of an excess, it will be necessary to:

- reduce the amount held in pension phase (e.g. a partial commutation) and
- pay excess transfer balance tax.

This applies for income streams that can be commuted (i.e. converted to a lump sum) such as an account based pension. The amount commuted must also include notional earnings (see below). The excess amount can be rolled back to the accumulation phase of superannuation or taken as a lump sum tax withdrawal. There is no limit to what you can maintain in a super accumulation account, so this option may enable you to maximise your investments in a concessional tax environment.

If non-commutable income streams (eg defined benefit pensions) are in excess of the transfer balance cap, the underlying capital cannot generally be removed to reduce the amount assessed against the cap. In such cases, excess transfer balance tax is not payable; however the taxation of the income stream payments is amended (see below).

The excess transfer balance tax is based on notional earnings determined by a legislative formula. Excess transfer balance tax is payable for all days where the amount held in pension phase of superannuation is in excess of the cap.

Notional earnings are subject to tax. In 2017/18 financial year, this additional tax is 15%. From 1 July 2018, the additional tax for the first breach of the cap will be 15% and subsequent breaches 30%.

If you exceed your transfer balance cap, adjustments to the pension can be made as soon as possible to minimise the excess transfer balance tax. If you are unaware or leave the funds in pension phase, the ATO will make a determination once the information from superannuation provider is received. Notional earnings will be calculated from the date of breach through to when a determination is made and that amount will then attract the General Interest Charge.

Once you have received a determination, the ATO provides you the opportunity to reduce the amount held in your pension by the amount in that determination. If you do not take the necessary steps, the ATO can provide a notice to your superannuation pension provider to make the necessary commutation on your behalf.

Non-commutable income streams exceeding the cap

Non-commutable income streams are assessed against the cap. The value of these income streams is determined by a legislative formula. In many cases, these income streams cannot be commuted if the assessment creates an excess against the transfer balance cap.

Where non-commutable income streams are in excess of the transfer balance cap, the taxation of the pension payments will change. The taxation of pension payment (income) above \$100,000 will be subject to different taxation compared to those amounts within the cap. The taxation is summarised below:

Type of scheme	Age	Amount below \$100,000 income cap	Amount above \$100,000 income cap
Taxed	< Preservation age	Taxed at marginal tax rate	Taxed at marginal tax rate
	> Preservation age - 59	Taxed at marginal tax rate less 15% offset	Taxed at marginal tax rate less 15% offset
	60 +	Tax-free	50% of amount above cap added to assessable income and taxed at marginal tax rate
Untaxed	< Preservation age	Taxed at marginal tax rate	Taxed at marginal tax rate
	> Preservation age - 59	Taxed at marginal tax rate	Taxed at marginal tax rate
	60 +	Taxed at marginal tax rate less 10% offset	Taxed at marginal tax rate

Transfer balance cap indexation

The transfer balance cap may be indexed in future years to CPI in \$100,000 increments. The extent that an individual benefits from indexation depends on whether that person has triggered a credit (or assessment) against their own transfer balance cap.

If a person has not triggered a credit against their transfer balance cap, they will benefit from the full increase of any indexation.

Those who have commenced an income stream but have not fully utilised the cap will have indexation applied only to the proportion of the unused transfer balance cap.

Indexation is not available for those who have completely utilised their transfer balance cap.

Risks and Consequences

- Commencing a superannuation income stream triggers an assessment against your transfer balance cap and the ATO will establish your transfer balance account.
- If the total amount used to commence superannuation income streams in retirement phase exceeds the cap, additional tax is payable.
- If you exceed the cap and have account based income streams, you are required to reduce the amount plus the notional earnings to ensure your transfer balance account reduces to at least \$1.6 million.
- If you exceed the cap and have non-account based income streams (such as defined benefit pension), certain tax concessions will no longer apply to the amount above \$100,000 pa.
- Death benefit pensions are also assessed against the transfer balance cap. Special rules apply to children.

- When you first commence a retirement phase income stream and the ATO establishes your transfer balance account, indexation of your cap will be limited to the unused portion. If you have utilised the full transfer balance cap, no indexation will apply to your cap.

Version: 1.00