LCR 2017/1 - Superannuation reform: capped defined benefit income streams - pensions or annuities paid from non-commutable, life expectancy or market linked products

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Superannuation reform: capped defined benefit income streams – pensions or annuities paid from non-commutable, life expectancy or market linked products

Relying on this Ruling

This Ruling is a public ruling for the purposes of the Taxation Administration Act 1953.

This Ruling describes how the Commissioner will apply the amendments made by the Treasury Laws Amendment (Fair and Sustainable Superannuation) Act 2016 (the Act) to entities that rely on it in good faith.

If you rely on this Ruling in good faith, you will not have to pay any underpaid tax, penalties or interest in respect of matters covered by the Ruling if it does not correctly state how a relevant provision applies to you.

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What this Ruling is about

1. This Ruling clarifies how the defined benefit income cap applies to superannuation income stream pensions or annuities that are paid from life expectancy or market linked products that are non-commutable.[1] The guidance follows changes made to the income tax treatment of certain defined benefit income stream benefits from the 2017-18 financial year.

2. All references are to the *Income Tax Assessment Act 1997*, unless otherwise stated.

Defined benefit income streams

3. Defined benefit income[2] is a superannuation income stream benefit[3] that is paid from a capped defined benefit income stream.[4]

4. This Ruling covers the following products that are non-commutable, capped defined benefit income streams, provided it was payable just before 1 July 2017:[5]

Product:	Provided the product is:
Life expectancy pension	a pension for the purposes of the *Superannuation Industry (Supervision) Act 1993 (*SISA) that is provided under rules that meet the standards of subregulation 1.06(7) of the *Superannuation Industry (Supervision) Regulations 1994* (SISR).[6]
Life expectancy annuity	an annuity for the purposes of the SISA that is provided under a contract that meets the standards of subregulation 1.05(9) of the SISR.[7]
Market linked pension	a pension for the purposes of the SISA that is provided under rules that meet the standards of subregulation 1.06(8) of the SISR.[8]
Market linked annuity	an annuity for the purposes of the SISA that is provided under a contract that meets the standards of subregulation 1.05(10) of the SISR.[9]

[1] Any reference in this Ruling to a superannuation income stream is limited to a life expectancy or market linked product that is not commutable as outlined in paragraph 4 of this Ruling, unless otherwise indicated.
[2] Subsection 303-2(2).
[3] Section 307-70 and subregulations 995-1.01(1) and (2) of the *Income Tax Assessment Regulations 1997*.
[4] Subsection 294-130(1) lists the capped defined benefit income streams.
[5] Paragraph 294-130(1)(b).
[6] Item 3 of the table in subsection 294-130(1).
[7] Item 4 of the table in subsection 294-130(1).
[8] Item 5 of the table in subsection 294-130(1).
[9] Item 6 of the table in subsection 294-130(1).

Market linked, RSA pension	a pension for the purposes of the *Retirement Savings Accounts Act 1997* that is provided under terms and conditions that meet the standards of subregulation 1.07(3A) of the *Retirement Savings Accounts Regulations 1997*.[10]

5. As with other types of superannuation income streams, the value of capped defined benefit income streams count towards your transfer balance cap. The transfer balance cap regime is designed to limit the amount of your superannuation that can be moved into the retirement phase, where it benefits from the fund earnings tax exemption.[11]

6. Capped defined benefit income streams cannot, of themselves, result in you having an excess transfer balance.[12] Instead, modifications to the general transfer balance cap rules apply.[13]

7. Instead of excess capped defined benefit income streams causing a breach of your transfer balance cap that needs to be remedied by removing the excess transfer balance, modifications result in certain amounts being included in assessable income and adjustments to the availability of tax offsets. The reason for the different treatment arises because capped defined benefit income streams generally cannot be commuted and cashed as a lump sum.

8. The following modifications apply for capped defined benefit income streams:

   (a) the application of a statutory formula to work out the value of your superannuation interest that supports a capped defined benefit income stream. This value is called the 'special value' and gives rise to a credit in your transfer balance account.[14]

   (b) the defined benefit income cap[15], which affects the defined benefit income that is included in your assessable income.[16] It also limits the tax offset available in respect of the untaxed element of certain benefits that are defined benefit income.[17]

Components of defined benefit income

9. A superannuation income stream benefit paid from a capped defined benefit income stream may consist of:

- a tax free component, and
- a taxable component.[18]

In turn, the taxable component of each superannuation benefit consists of either or both of:

- an element taxed in the fund (taxed element), or

[10] Item 7 of the table in subsection 294-130(1).
[11] The transfer balance cap regime is contained in Division 294.
[12] Section 294-140.
[13] Refer to LCR 2016/9 *Superannuation reform: transfer balance cap* for additional guidance about the transfer balance cap.
[14] Section 294-135. Special rules also apply for determining transfer balance debits (equal to their 'debit value') for capped defined benefit income streams. The most common way that a debit arises in a transfer balance account is due to the full or partial commutation of a relevant income stream. However, as set out at paragraph 1 of this Ruling, this Ruling applies only to certain capped defined benefit income streams that are non-commutable. Therefore, this Ruling does not discuss debits. Further explanation of the debit value of a commutation debit is contained at paragraph 3.232 (and following) of the Explanatory Memorandum (EM) to the *Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016* (the Bill).
[15] Section 303-4.
[16] Section 303-2.
[17] Section 303-3.
[18] Sections 294-130, 307-70 and 307-120. The tax free component may be nil.

- an element untaxed in the fund (untaxed element).[19]

These terms are relevant for applying the defined benefit income cap.

Special value of a superannuation interest

10. If a pension or annuity from a life expectancy or market linked product is payable to you, a credit arises in your transfer balance account. This credit equals the 'special value' of the superannuation interest that supports your superannuation income stream.[20]

11. The special value of a superannuation interest that supports your pension or annuity from a life expectancy or market linked product is calculated by multiplying the 'annual entitlement' by the product's 'remaining term'.[21]

12. The 'annual entitlement' is worked out by annualising the first superannuation income stream benefit you are entitled to receive from the income stream across a year.[22] The annual entitlement amount will correspond to the amount required to be paid during the year in accordance with the agreement under which the life expectancy or market linked product is provided and the relevant regulatory provisions.[23] The first superannuation income stream benefit you are entitled to receive comprises all of its constituent components (for example, all of its tax free component, and taxable component (taxed elements and/or untaxed elements)).

13. The 'remaining term' is the number of years remaining in the period throughout which superannuation income stream benefits are payable under a product (rounded up to the next whole number).

14. [Omitted.]

15. If a pension or annuity from a life expectancy or market linked product is payable to you prior to 1 July 2017, the credit that arises in your transfer balance account is equal to the special value of the superannuation interest that supports that income stream just before 1 July 2017 (being the end of 30 June 2017). The credit arises in your transfer balance account on 1 July 2017.[25] The special value will be calculated based on the first superannuation income stream benefit that you are entitled to receive on or after 1 July 2017.

15A. If an individual who is being paid a life expectancy or market linked pension or annuity prior to 1 July 2017 dies and the pension or annuity then becomes payable to you as a reversionary beneficiary on or after 1 July 2017, the credit that arises in your transfer balance account is equal to the special value of the superannuation interest that supports that income stream on the date the income stream first becomes payable to you (the starting day). However, the credit arises in your transfer balance account 12 months from the starting day.[25A]

Example 1: Special value of a superannuation interest

16. *Just before 1 July 2017, Victoria has a market linked pension. The first benefit she is entitled to receive from her pension just after that time is her fortnightly payment of*

[19] Section 307-275.
[20] Subsections 294-135(1) and (3) .
[21] Subsection 294-135(3).
[22] Subsection 294-135(3), which refers to the 'annual entitlement' definition in subsection 294-135(2).
[23] See paragraphs 1.05(9)(c), 1.05(9)(d), 1.05(10)(b), 1.06(7)(c), 1.06(7)(d) and 1.06(8)(b) of the SISR and paragraph 1.07(3A)(b) of the conditions that meet the standards of subregulation 1.07(3A)(b) of the *Retirement Savings Accounts Regulations 1997*.
[24] [Omitted.]
[25] Item 1 of the table in subsection 294-25(1).
[25A] See Column 4 of Item 1 in the table in subsection 294-25(1).

$2,301.37 due on 4 July 2017. The remaining term in Victoria's pension just before 1 July 2017 is 9.75 years.

17. *Victoria's annual entitlement just before 1 July 2017 is $60,000[26], which is worked out as follows:*

$$\frac{\text{First payment}}{\text{Days in period}} \times 365$$

$$= \frac{\$2{,}301.37}{14} \times 365$$

$$= \$60{,}000$$

18. *The remaining term in Victoria's pension just before 1 July 2017 is rounded up from 9.75 years to 10 years (being the next whole number) when determining the pension's special value.*

19. *The special value of Victoria's pension just before 1 July 2017 is $600,000 ($60,000 x 10 years). A credit arises in Victoria's transfer balance account on 1 July 2017 for this amount.*

Excess transfer balance

20. For non-commutable defined benefit income streams any potential excess transfer balance is not able to be remedied by commutation. If a capped defined benefit income stream is payable to you, then you will only have excess transfer balance if the balance in your transfer balance account exceeds both your transfer balance cap[27] and your capped defined benefit balance.[28]

21. Your capped defined benefit balance is the net sum of the transfer balance credits and debits in your transfer balance account for capped defined benefit income streams.[29] If you only have a capped defined benefit income stream, the transfer balance in your transfer balance account can never exceed your capped defined benefit balance. You will therefore not have an excess transfer balance regardless of whether the special value of the superannuation interest that supports your capped defined benefit income stream exceeds your transfer balance cap.

22. An individual may have both a capped defined benefit income stream and another type of superannuation income stream (for example, an account-based pension). That individual may exceed both their transfer balance cap and their capped defined benefit balance. If this applies to you, either a full or partial commutation of the other superannuation income stream is required to be made to reduce the balance of your transfer balance account below your transfer balance cap. However, where the value of

[26] This amount corresponds with the annual amount required to be paid under the market linked pension in accordance with paragraph 1.06(8)(b) of the SISR.
[27] An individual's transfer balance cap for the 2017–18 financial year is $1.6 million (section 294-35). Also see LCR 2016/9 *Superannuation reform: transfer balance cap*.
[28] Subsection 294-140(1).
[29] Subsection 294-140(3).

the superannuation interest supporting the other superannuation income stream is reduced to nil (for example, by paying superannuation income stream benefits or due to fund losses) so that you only have the capped defined benefit income stream, the Commissioner will issue a notice to you.[30] At the time the Commissioner issues the notice, a debit arises in your transfer balance account equal to the amount of the excess transfer balance stated in the notice.[31] In this way, you will cease to have excess transfer balance in your transfer balance account.

Defined benefit income cap

23. The defined benefit income cap is relevant where you are:

    (a) 60 years of age or over, or

    (b) under 60 years of age and a death benefits dependant, where the deceased died at 60 years of age or over.

The defined benefit income cap applies, if you receive one or more superannuation income stream benefits that are 'defined benefit income' to which 'concessional tax treatment'[32] applies (see paragraph 32 of this Ruling). The defined benefit income cap does not have taxation consequences outside of these circumstances.

24. The defined benefit income cap is an annual cap that is reset, and may be reduced, each year. These circumstances are discussed in paragraphs 25 to 31 of this Ruling.

Defined benefit income cap threshold

25. Your defined benefit income cap is the general transfer balance cap for the financial year divided by 16.[33] For example, as the general transfer balance cap for the 2017–18 financial year is $1.6 million, the defined benefit income cap is $100,000.

26. However, your defined benefit income cap is reduced where you first become entitled to concessional tax treatment (see paragraph 32 of this Ruling) part way through a financial year[34], or you receive defined benefit income that is not subject to concessional tax treatment.[35]

27. The defined benefit income cap is not increased for proportional indexation.[36] However, it will increase over time because it is based on the general transfer balance cap, which is indexed.[37] As the defined benefit income cap is based on the general (not an individual's) transfer balance cap, this indexation is not lost if you meet or exceed your personal transfer balance cap.

Part-year reduction of the defined benefit income cap

28. Where an individual starts to receive defined benefit income part way through a financial year, then the defined benefit income cap is pro-rated for the remaining part of the financial year using the following formula (rounded up to the nearest dollar):[38]

[30] The notice is issued under section 136-70 of Schedule 1 to the *Taxation Administration Act 1953.*
[31] Item 7 of the table in section 294-80.
[32] The reference to 'concessional tax treatment' is consistent with the terminology used in the EM to the Bill (for example, see paragraph 3.250 of the EM).
[33] Subsection 303-4(1).
[34] Subsection 303-4(2).
[35] Subsection 303-4(3).
[36] Section 294-40.
[37] Subsection 294-35(3).
[38] Subsection 303-4(2).

$$\frac{\text{The general transfer balance cap for the financial year}}{16} \times \frac{\text{1+ number of days remaining in the financial year after that day}}{\text{Number of days in the financial year}}$$

Example 2: Defined benefit income cap – part-year reduction

29. *Greg is receiving a life expectancy annuity which commenced before 1 July 2017. The annuity has an initial, annual entitlement of $150,000 and is sourced entirely from a taxed element. Greg turns 60 on 1 January 2018, and receives an annuity payment on that date.*

30. *Greg first becomes entitled to concessional tax treatment on 1 January 2018.*[39] *His defined benefit income cap is pro-rated for the 2017-18 financial year, in accordance with the formula above, as follows:*

$$\frac{\$1.6 \text{ million}}{16} \times \frac{1 + 180 \text{ days}}{365}$$

Greg's defined benefit income cap will be $49,590 for the 2017–18 financial year.

Reduction where some defined benefit income is not subject to concessional tax treatment

31. The defined benefit income cap is also reduced, where you receive **both** of the following types of defined benefit income during a financial year:

(i) defined benefit income that is subject to concessional tax treatment (see paragraph 32 of this Ruling), and

(ii) defined benefit income that is not subject to concessional tax treatment.[40]

If you receive both these types of income during a financial year, you reduce your defined benefit income cap for the year. The cap is reduced by the defined benefit income that is not subject to concessional tax treatment. This reduction is made after any part-year reduction of the defined benefit income cap as described at paragraph 28 of this Ruling. See Example 6 of this Ruling.

Concessional taxation treatment

32. References in this Ruling to 'concessional tax treatment' of defined benefit income are as follows:

(a) The tax free component of a superannuation income stream benefit that is defined benefit income is non-assessable, non-exempt income if you are:

(i) 60 years of age or over[41], or

(ii) under 60 years of age and in receipt of a death benefit, where the deceased died at 60 years of age or over.[42]

[39] Section 301-10.
[40] Subsection 303-4(3).
[41] Sections 301-10 and 302-65.
[42] Section 302-65.

(b) The taxed element of a superannuation income stream benefit that is defined benefit income is non-assessable, non-exempt income if you are:

(i) 60 years of age or over[43], or

(ii) under 60 years of age and in receipt of a death benefit, where the deceased died at 60 years of age or over.[44]

(c) The untaxed element of a superannuation income stream benefit that is defined benefit income is included in your assessable income. You are entitled to a tax offset equal to 10% of the untaxed element if you are:

(i) 60 years of age or over[45], or

(ii) under 60 years of age and in receipt of a death benefit, where the deceased died at 60 years of age or over.[46]

Consequences of exceeding the defined benefit income cap

33. The consequence of you exceeding your defined benefit income cap is that:

(a) additional amounts of defined benefit income that would otherwise be non-assessable, non-exempt income, may be included in your assessable income, and/or

(b) the tax offsets otherwise available to you, in respect of any untaxed element of your defined benefit income, may be reduced.

Additional assessable income

34. Where the sum of the tax free component and taxed element of benefits that are defined benefit income and non-assessable, non-exempt income as described in paragraph 32 of this Ruling, exceeds your defined benefit income cap, 50% of the excess is assessable income (to which no tax offset applies).[47]

35. PAYG withholding obligations will apply to these payments.[48]

Example 3: Capped defined benefit income stream – tax free component and taxed element

36. *Sally is 67 during the 2017-18 financial year and is receiving a life expectancy pension which commenced before 1 July 2017. The pension qualifies as a capped defined benefit income stream, and is comprised entirely of a tax free component and a taxed element.*

37. *For the 2016–17 financial year, Sally's pension income is non-assessable, non-exempt income.*

38. *For the 2017–18 financial year, Sally receives $150,000 under the pension. The sum of the benefits comprising the tax free component and taxed element[49] exceeds her $100,000 defined benefit income cap. Therefore, Sally includes in her assessable income 50% of the defined benefit income that exceeds her defined benefit income cap.*

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[43] Section 301-10 and 302-65.
[44] Section 302-65.
[45] Sections 301-100 and 302-85.
[46] Section 302-85.
[47] Section 303-2.
[48] Subsection 12-1(4) and section 12-80 in Schedule 1 of the *Taxation Administration Act 1953,* and the EM to the Bill at paragraph 3.302. PAYG withholding schedules will be updated to reflect the amendments.
[49] That is, the amounts to which section 301-10 applies.

39. *As $50,000 of her pension exceeds her defined benefit income cap, she includes $25,000 in her assessable income for the 2017–18 financial year. Sally is not entitled to a tax offset in relation to this income. Sally needs to declare this income by lodging an individual income tax return, and she may have an income tax liability for the 2017–18 financial year.*

Reduced tax offset

40. Where:

    (a) you are entitled to tax offset(s) in respect of the untaxed element of a defined benefit income stream as described in paragraph 32(c) of this Ruling, and

    (b) the sum of the non-assessable, non-exempt income amounts described at paragraphs 32(a) and (b) of this Ruling, and the assessable amounts described at paragraph 32(c) of this Ruling, exceeds your defined benefit income cap for a financial year,

the sum of those tax offsets for the year is reduced by 10% of that excess. But, the tax offsets cannot be reduced below zero.

Example 4: Capped defined benefit income stream – tax free component and untaxed element

41. *Alastair is 68 and is receiving a life expectancy pension of $160,000 per annum which commenced before 1 July 2016. The pension is a capped defined benefit income stream and is comprised of a tax free component of $60,000, and an untaxed element of $100,000. Alastair's defined benefit income cap for a financial year is $100,000.*[50]

Tax free component

42. *The sum of the benefits comprising the tax free component and the taxed element ($60,000) does not exceed Alastair's defined benefit income cap. From the 2017–18 financial year, Alastair has no additional amount included in his assessable income. The $60,000 tax free component of Alastair's pension is non-assessable, non-exempt income for the 2016–17 and 2017–18 financial years.*

Untaxed element

43. *For the 2016–17 financial year, Alastair includes the $100,000 untaxed element of his pension in his assessable income and claims a 10% tax offset ($10,000).*

44. *For the 2017–18 financial year, Alastair includes the $100,000 untaxed element of his pension in his assessable income. The total amount of Alastair's defined benefit income (the sum of the tax free component, taxed element and untaxed element*[51]*) ($160,000) exceeds his defined benefit income cap of $100,000. Accordingly, his $10,000 tax offset is reduced by $6,000 (being 10% of the $60,000 excess). Alastair's tax offset for the 2017-18 financial year is therefore $4,000.*

[50] For the purposes of illustration in this example, the amount paid under the life expectancy pension remains the same from 1 July 2016 to 30 June 2018.
[51] That is, the amounts to which sections 301-10 and 301-100 apply.

Example 5: Capped defined benefit income stream – part-year reduction - tax free component and taxed element

45. *Mary receives a life expectancy annuity of $150,000 per annum. Her annuity is a capped defined benefit income stream that is comprised of a tax free component of $50,000, and a taxed element of $100,000.*

46. *Mary's annuity started before 1 July 2016, and she turns 60 on 12 September 2017. Mary received 80% of her annuity for the 2017–18 financial year after turning 60 (that is, a $40,000 tax free component, and an $80,000 taxed element).*[52]

47. *Both before and after the changes, the income Mary received before turning 60 years of age, but above her preservation age, for the 2017–18 financial year is treated as follows.*

- *the $10,000 tax free component is non-assessable, non-exempt income, and*
- *the $20,000 taxed element is included in her assessable income and she is entitled to a tax offset of 15% of this income ($3,000).* [53]

48. *Before the changes, the income Mary received after turning 60 would have been treated as follows:*

- *the $40,000 tax free component was non-assessable, non-exempt income, and*
- *the $80,000 taxed element was non-assessable, non-exempt income.*

49. *In applying the changes from when Mary turns 60, Mary's defined benefit income cap is reduced. The reduction reflects the period during the 2017–18 financial year that her annuity was subject to concessional tax treatment (that is, the period from when she turned 60).*

50. *Mary's defined benefit income cap for the 2017–18 financial year is calculated as follows.*

$$\frac{\text{The general transfer balance cap for the financial year}}{16} \times \frac{\text{1+ number of days remaining in the financial year after that day}}{\text{Number of days in the financial year}}$$

$$= \frac{\$1.6\text{ million}}{16} \times \frac{1 + 291\text{ days}}{365}$$

Mary's defined benefit income cap will be $80,000 for the 2017–18 financial year.

The sum of the tax free component and taxed element of Mary's annuity income that received concessional tax treatment ($120,000), exceeds her reduced defined benefit income cap ($80,000). Therefore, Mary includes $20,000 in her assessable income for the 2017–18 financial year (being 50% of the $40,000 excess).

51. *As Mary is over 60 for the entire 2018–19 financial year, all of her annuity is subject to the defined benefit income cap. No part year reduction will apply for this year.*

[52] For the purposes of illustration in this example, the amount paid under the life expectancy annuity remains the same from 1 July 2016 to 30 June 2018.
[53] Sections 301-15 and 301-25.

Example 6: Capped defined benefit income stream and a concessional reversionary death benefit income stream

52. *Ann turns 59 on 1 July 2017, and has been receiving a life expectancy pension of $130,000 per annum. Her life expectancy pension is a capped defined benefit income stream that is comprised of a tax free component of $60,000, a taxed element of $40,000, and an untaxed element of $30,000. Ann receives 80% of her life expectancy pension for the 2017-18 financial year after 12 September 2017.*

53. *Ann's spouse David dies on 12 September 2017 aged 65. She begins receiving a reversionary pension on 12 September 2017 of $75,000 per annum. It is a capped defined benefit income stream, with a tax free component of $50,000, and an untaxed element of $25,000. From 12 September 2017 to 30 June 2018, Ann received $60,000 in reversionary pension payments, of which $40,000 constituted a tax free component, and $20,000 was an untaxed element.*[54]

Treatment of Ann's life expectancy pension: 2016–17 and 2017–18 financial years – when she is under age 60

54. *The income Ann receives from her life expectancy pension before turning 60 years of age, but above her preservation age, is treated as follows:*

- *the $60,000 tax free component is non-assessable, non-exempt income*
- *the $40,000 taxed element is included in her assessable income and Ann is entitled to a tax offset of 15% of this income ($6,000), and*
- *the $30,000 untaxed element is included in her assessable income and there is no tax offset in relation to this income.*

55. *This treatment applies for both the 2016–17 and 2017–18 financial years.*

56. *None of this income receives the concessional tax treatment referred to in paragraph 32.*[55]

Treatment of Ann's reversionary pension: 2017–18 financial year – when she is under age 60

57. *The income Ann receives from her reversionary pension is treated as follows:*

- *the $40,000 tax free component is non-assessable, non-exempt income, and*
- *the $20,000 untaxed element is included in her assessable income, and she is entitled to a tax offset of 10% of this income ($2,000).*

If Ann had received the reversionary pension during the 2016–17 financial year, this would have been the tax treatment that applied.

58. *For the 2017-18 financial year, the changes to the law result in Ann having to include an additional $20,000 in her assessable income, and her $2,000 tax offset is also reduced to nil. The reasons for this changed treatment are as follows.*

59. *Although Ann is not yet aged 60, the defined benefit income she received from her reversionary pension was subject to concessional tax treatment for the 2017–18 financial*

[54] For the purposes of illustration in this example, the amounts paid under Ann's income streams remain the same, as relevant, from 1 July 2016 to 30 June 2019.
[55] Sections 301-10 and 301-100.

year.[56] Therefore, the defined benefit income cap applies to the defined benefit income she received for that year.

60. *The defined benefit income cap for the 2017–18 financial year is $100,000. However, Ann's defined benefit income cap is reduced because the 2017-18 financial year was the first year she became entitled to concessional tax treatment (the reversionary pension). She also received income that was not subject to concessional tax treatment (the life expectancy pension). The reduction reflects:*

(a) the period in the 2017–18 financial year that her reversionary pension was subject to concessional tax treatment, and

(b) the life expectancy pension she received that was not subject to concessional tax treatment.

61. *Ann commenced receiving her reversionary pension on 12 September 2017, so her reduced defined benefit income cap is $80,000 (see Example 5 of this Ruling for an explanation). However, Ann also received defined benefit income that was not subject to concessional tax treatment in the 2017–18 financial year. This means that Ann's defined benefit income cap is further reduced as follows:*

$80,000 - (the amount of Ann's $130,000 life expectancy pension received after 12 September 2017)

= $80,000 - (80% x $130,000)

= $80,000 - $104,000

= negative $24,000

The effect of Ann having a reduced defined benefit income cap that is negative is that her defined benefit income cap is nil for the 2017–18 financial year.

62. *The amount of Ann's reversionary pension excluding the untaxed element is $40,000 for the 2017–18 financial year. This exceeds her defined benefit income cap for the year (nil). She will need to include an additional $20,000 in her assessable income for the 2017–18 financial year (being 50% of the $40,000 excess).*

63. *Ann's total reversionary pension receipts for the 2017-18 financial year ($60,000) exceed her defined benefit income cap (nil) for the year. Therefore, she must reduce her $2,000 tax offset by $6,000 (being 10% of that excess). The reduction exceeds Ann's tax offset, so she is not entitled to any tax offset for the 2017–18 financial year.*

<u>Treatment of Ann's income streams for the 2018–19 financial year</u> – <u>when she is 60</u>

64. *Ann turns 60 on 1 July 2018. Before any adjustments under the changes, Ann's life expectancy pension is treated as follows for the 2018-19 financial year:*

- *the $60,000 tax free component is non-assessable, non-exempt income*
- *the $40,000 taxed element is non-assessable, non-exempt income, and*
- *the $30,000 untaxed element is included in her assessable income and Ann is entitled to a tax offset of 10% on this income ($3,000).*

65. *Ann's reversionary pension is treated as follows for the 2018–19 financial year, before any adjustments under the changes:*

- *the $50,000 tax free component is non-assessable, non-exempt income, and*

[56] Sections 302-65 and 302-85.

- *the $25,000 untaxed element is included in her assessable income, and she is entitled to a tax offset of 10% of this income ($2,500).*

66. *Ann's defined benefit income cap for the 2018–19 financial year is $100,000. The cap is not reduced because all of her defined benefit income is subject to concessional tax treatment.*

67. *The sum of Ann's defined benefit income excluding the untaxed elements she receives is $150,000 ($60,000 + $40,000 + $50,000). This exceeds her cap by $50,000. The changes to the law result in Ann having to include an additional $25,000 in her assessable income for the 2018–19 financial year (being 50% of the $50,000 excess).*

68. *Ann's tax offsets for the untaxed elements of her pensions, before any adjustment, total $5,500 for the 2018–19 financial year ($3,000 + $2,500). However, her tax offset entitlement is reduced. This is because the sum of Ann's defined benefit income that is subject to concessional tax treatment for the 2018-19 financial year is $205,000 ($130,000 + $75,000), which exceeds her defined benefit income cap for the year by $105,000. Her tax offsets will be reduced by $10,500 (being 10% of the $105,000 excess). Ann's tax offsets totalling $5,500 will be reduced to nil for the 2018–19 financial year.*

Commissioner of Taxation
28 April 2017

References

ATOlaw topic(s)	Superannuation ~~ Income tax - individuals (superannuation) ~~ Other
Legislative references	ITAA 1997 ITAA 1997 Div 294 ITAA 1997 294-25(1) ITAA 1997 294-35 ITAA 1997 294-35(3) ITAA 1997 294-40 ITAA 1997 294-80 ITAA 1997 294-130 ITAA 1997 294-130(1) ITAA 1997 294-130(1)(b) ITAA 1997 294-135 ITAA 1997 294-135(1) ITAA 1997 294-135(2) ITAA 1997 294-135(3) ITAA 1997 294-140 ITAA 1997 294-140(1) ITAA 1997 294-140(3) ITAA 1997 301-10 ITAA 1997 301-15 ITAA 1997 301-25 ITAA 1997 301-100 ITAA 1997 302-65 ITAA 1997 302-85 ITAA 1997 303-2 ITAA 1997 303-2(2) ITAA 1997 303-3 ITAA 1997 303-4 ITAA 1997 303-4(1) ITAA 1997 303-4(2) ITAA 1997 303-4(3) ITAA 1997 307-70 ITAA 1997 307-120 ITAA 1997 307-275 TAA 1953 TAA 1953 Sch 1 136-70 TAA 1953 Sch 1 12-1(4) TAA 1953 Sch 1 12-80 ITAR 1997 ITAR 1997 995-1.01(1) ITAR 1997 995-1.01(2) Retirement Savings Accounts Act 1997 Treasury Laws Amendment (Fair and Sustainable Superannuation) Act 2016 Superannuation Industry (Supervision) Act 1993 Superannuation Industry (Supervision) Regulations 1994 Retirement Savings Accounts Regulations 1997
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