2019/20 FEDERAL BUDGET REPORT

FIN SEC PARTNERS

April 2019

A Budget for the political times tempered by the economic times, is the underlying theme for Budget 2019.

With Scott Morrison to call the election within a matter of days, Treasurer Josh Frydenberg had to pull a rabbit out of the hat last week and we'll know by election day whether it's a live one or not. The strategy was simple; reinforce the Government's superior economic management with cash hand-outs, restoring the surplus and covering essential services all without having to increase taxes. Effectively the scene has been set for a tax stoush all the way through the election campaign.

So, what to make of the actual budget measures? From a financial services perspective, not a lot and after a year of Hayne royal commission there isn't much the Government can announce that would shock us. In-fact the big story for us was more about 'what was not included'. No mention of unfunded Age Pension liabilities (a very real and global problem over the next 20 to 30 years) or the impact of baby boomers retiring. A phenomenon that the Budget Office itself proclaims will see revenue fall by around $20 billion and spending increase by $16 billion to 2031.

But let's face it, no real surprise there - "No pain, no gain" budgets (Joe Hockey, Budget 2014) don't have a great track record when it comes to winning over the public or winning elections.

The majority of you will have read the facts and figures and by now will have an understanding of the proposed measures. Normally our summary would not be a simple reiteration of these facts, however this year (from a financial planning perspective) there is so little that the normal ambiguities are distinctly missing. None-the-less we seek to report on all the relevant measures with clarity and where appropriate have included a FinSec comment.

We trust that you enjoy the read and we look forward to speaking with you individually about how this budget may impact your personal circumstances.

SUPERANNUATION

While compared to prior years the Superannuation announcements were minimal and largely positive in nature, there were some important changes which impact Superannuation funds and their members.

Budget recommendations include:

1 Improved flexibility to the work test rules

Proposed effective date: 1 July 2020
Who this affects: Australians aged 65-74 who have recently ceased work and have super balances below $1.6 million

Currently, individuals aged 65 to 74 can make voluntary superannuation contributions only if they work at least 40 hours over a 30 day period in the relevant financial year.

From 1 July 2020, the Government has announced that voluntary contributions (both concessional and non-concessional) can be made by those aged 65 and 66 without meeting the work test. You can also make up to three

years of non-concessional contributions (currently capped at $100,000 a year) under the bring-forward rule.

This measure is intended to align the work test with the eligibility age for the Age Pension (scheduled to reach 67 from 1 July 2023).

FinSec Comment

For those with access to the resources to take advantage of this change it could be extremely powerful. This measure provides individuals who have built wealth outside of superannuation with a larger window to execute estate planning strategy involving the taxable component of super. What's more it provides the potential to crystallise capital gains in the year after retirement and contribute those gains to superannuation.

On the flip side we question whether individuals who are no longer working many hours, if at all, and have small superannuation balances are likely to have large sums of money to contribute to their super account.

2 Increase in the age limit for spousal contributions

Proposed effective date: 1 July 2020
Who this affects: Australian Retirees aged 70 to 74

Currently, Retirees aged 70 and over cannot receive spousal contributions.

Under proposed new rules the age limit will be increased to 74 giving older Australians greater flexibility to save for retirement.

FinSec Comment

Whilst there will be very few people in a position to take advantage of this change for those who can it is a "nice to have".

3 Permanent tax relief for merging superannuation funds

Proposed effective date: 1 July 2020
Who this affects: Superannuation fund members

A previous change due to expire on 1 July 2020 is now made permanent to make it easier for super funds to merge. Since December 2008, tax relief has been available for superannuation funds to transfer revenue and capital losses to a new merged fund, and to defer taxation consequences on gains and losses from revenue and capital assets.

The tax relief will be made permanent from 1 July 2020. The measure will help address inefficiencies by reducing costs, managing risks and increasing scale, leading to improved retirement outcomes for members.

FinSec Comment

ASIC has been pushing for rationalisation in the industry so this move makes sense. It ensures members are not adversely affected by taxation consequences (such as realising capital gains) when funds merge. The move is also consistent with the recommendation of the Productivity Commission's final report into the superannuation industry.

At FinSec we would like to see similar collaboration between the ATO and Centrelink whereby institutions and/or clients can consolidate their product suites without creating tax issues or compromising Centrelink grandfathering and/or insurance benefits.

4. Streamlining administrative requirements for the calculation of Exempt Current Pension Income

Proposed effective date: 1 July 2020
Who this affects: Superannuation fund trustees

The Government will reduce costs and simplify reporting for superannuation funds by streamlining some administrative requirements for the calculation of Exempt Current Pension Income (ECPI).

The Government will allow superannuation fund trustees with interests in both the accumulation and retirement phases during an income year to choose their preferred method of calculating ECPI.

The Government will also remove a redundant requirement for superannuation funds to obtain an actuarial certificate when calculating ECPI using the proportionate method, where all members of the fund are fully in the retirement phase for all of the income year.

This measure is estimated to have no revenue impact over the forward estimates period.

FinSec Comment

A welcome initiative and one that the SMSF sector advocated for in it's Budget submission. This change reduces administrative red tape and helps to control the cost of running a SMSF.

5. Protecting your super package – Active accounts

Proposed effective date: 1 July 2019
Who this affects: Superannuation fund members with balances below $6000

The Government has announced it will extend the period after which a superannuation account has not received contributions, and is thus considered inactive, to 16 months (currently 13 months) and will expand the definition of when an account is considered active "for the ATO-led consolidation regime" mandating that the ATO consolidate active accounts, where possible, within 28 days.

FinSec Comment

There is no doubt that excess fees and premiums paid by individuals with unintended multiple accounts do have a detrimental impact on their retirement balance. Perversely, as accounts are removed from funds we could see the average fee increase i.e. currently inactive accounts are cross subsidising active accounts (the cost of administering an inactive account is much lower) and, fewer accounts means less in "the pool" to spread across the fixed costs of administration.

The change in definition of an inactive account from 13 - 16 months is welcomed as it gives individuals an additional 3 months to get their affairs in order. However, when it comes to inactive and lost accounts 'prevention is definitely better than the cure'. We implore all individuals, particularly women who take extended breaks from the workforce, to minimise the risk of having to navigate this space. Taking action can be as simple as ensuring your details (in particular your address) are kept up to date.

6. Protecting your super package – Delay to insurance opt-in

Proposed effective date: Delayed from 1 July 2019 to 1 October 2019
Who this affects: Australians under 25 and super balances with less than $6000

The Government has announced it is delaying the start date for ensuring super funds only offer insurance on an opt-in basis - at least for accounts with balances of less than $6000 or new accounts belonging to under 25s to October 1st, 2019 (currently 1 July, 2019).

The changes will protect the retirement savings of young people and those with low balances by ensuring their superannuation is not unnecessarily eroded by premiums on insurance policies they do not need or are not aware of.

These changes will not prevent individuals who want insurance from being able to obtain it — low balance and young members will still be able to opt in to insurance cover within superannuation.

FinSec Comment

We agree that it is not fair for young people with low balances and no need for insurance to be paying for something they neither need or even know they have. However, much like with multiple super accounts, their insurance premiums have over time reduced the overall premium cost to the entire "pool". Consequently an unforeseen outcome of this change may be an increase in insurance premium for those who do opt-in. Compounding this further will be the fact that those most likely to opt-in will be the funds high risk members (older, health problems etc.).

7. Possible establishment of a Superannuation Consumer Advocate

The Government will undertake an expression of interest process to identify options to support the establishment of a Superannuation Consumer Advocate. The Advocate would represent consumers on policy discussions and also provide educational information and assistance to consumers in relation to the superannuation system.

FinSec Comment

FinSec endorses any initiative that raises financial literacy and peoples interest in what will inevitably become one of their largest assets and wealth accumulation vehicles.

THE ROYAL COMMISSION

The Government will provide $606.7 million over five years from 2018-19 to facilitate its response to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

The package comprises a suite of measures that fulfil the Government's commitment to take action on all 76 of the recommendations of the royal commission's final report.

Budget recommendations include:

- Designing and implementing an industry funded compensation scheme of last resort for consumers and small business ($2.6 million over two years from 2019-20);
- Providing the Australian Financial Complaints Authority with additional funding to help establish a historical redress scheme to consider eligible financial complaints dating back to 1 January 2008 ($2.8 million in 2018-19);

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- Paying compensation owed to consumers and small businesses from legacy unpaid external dispute resolution determinations ($30.7 million in 2019-20);
- Resourcing ASIC to implement its new enforcement strategy and expand its capabilities and roles in accordance with the recommendations of the royal commission ($404.8 million over four years from 2019-20).
- Resourcing the Australian Prudential Regulation Authority (APRA) to strengthen its supervisory and enforcement activities, which will support its response to key areas of concern raised by the royal commission, including with respect to governance, culture and remuneration ($145.0 million over four years from 2019-20);
- Establishing an independent financial regulator oversight authority, to assess and report on the effectiveness of ASIC and APRA in discharging their functions and meeting their statutory objectives ($7.7 million over three years from 2020-21);
- Undertaking a capability review of APRA, which will examine its effectiveness and efficiency in delivering its statutory mandate, as well as its capability to respond to the royal commission ($1.0 million in 2018-19);
- Establishing a Financial Services Reform Implementation Taskforce within the Treasury to implement the Government's response to the royal commission, and co-ordinate reform efforts with APRA, ASIC and other agencies through an implementation steering committee ($11.2 million in 2019-20); and
- Providing the Office of Parliamentary Counsel with additional funding for the volume of legislative drafting that will be required to implement the Government's response to the royal commission ($0.9 million in 2019-20). The cost of this measure will be partially offset by revenue received through ASIC's industry funding model and increases in the APRA Financial Institutions Supervisory Levies and from funding already provisioned in the budget.

FinSec Comment

As we have previously opined, the issues raised by the Royal commission were heinous and must be addressed by all stakeholders in the industry quickly and decisively. It is critical however that consultation and collaboration between the stakeholders is robust and constructive to ensure that the changes ultimately introduced actually achieve the outcomes they are seeking to deliver. There is a risk of overreach when such emotive issues are addressed with political expediency in mind.

AGED CARE AND PENSION

The Government also made a pitch for the votes of families and older Australians with new spending in aged care and a promise to make Medicare more affordable and services more accessible.

Budget recommendations include:

- A one off, income tax exempt payment of $75 for singles and $125 for couples who were on a qualifying payment on 2 April 2019. The payment is to help assist with "their next power bill" and cost of living expenses. Qualifying payments include:
  - Age Pension/Service Pension
  - Carer Payment
  - Disability Support Pension
  - Parenting Payment Single, and
  - DVA War Widow(er)s Pension, Income Support Supplement, and disability payments;

- Providing the Commonwealth Home support Programme (CHSP) with extended funding. The CHSP is entry level support services and personal care at home. The CHSP can include services such as meals, nursing care, home maintenance, home modifications, aids and equipment (e.g. mobility aids) and/or community transport to assist older people to keep living independently in their own home;

- Additional funding for the addition of 13,500 residential aged care places;

- Additional funding from 2018-19 over five years for the release of an additional 10,000 home care packages across the four package levels. This would bring the total of additional home care packages introduced since 2017-18 to 40,000.

- Resourcing an increase to the dementia and veterans' home care supplements from 2018-19 over five years. This measure aims to assist eligible home care recipients who require additional care to stay in their home longer.

  The veterans' home care supplement provides additional funding for veterans with a mental health condition accepted by the Department of Veterans' Affairs (DVA) as related to their service. The dementia and cognition supplement provides additional funding to acknowledge the extra costs of caring for people with cognitive impairment associated with dementia and other conditions.

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