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Technically Speaking: Unpacking Division 296 Tax

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Overview

There has been a great deal of focus and attention placed on the necessity and fairness of, as well as the complexity associated with, the introduction of a new tax on superannuation earnings for those with superannuation balances greater than $3,000,000.

With the Government having recently introduced the Treasury Laws Amendment (Better targeted superannuation concessions and other measures) Bill 2023, the time has come to start developing a deeper understanding of the mechanics that will underpin this new tax, should it become law.

The abovementioned Bill proposes to introduce new Division 296 into the Income Tax Assessment Act (ITAA) – as such, this new tax is likely to become affectionately known as Division 296 tax.

This proposed new tax, which will come into operation from the 2025-26 financial year (and onwards) will broadly impact on those who, at the end of the relevant financial year, have a TSB greater than $3,000,000.

While this may appear relatively straightforward, there are a number of complexities that arise when calculating an individual's potential tax liability.

For instance, complexities arise where an individual first enters into the realm of this new tax, that is, where their TSB at the end of a financial year first exceeds $3 million. Similarly, complexity arises where an individual's TSB, which was previously greater than $3,000,000, falls below this threshold at the end of a financial year – meaning they are not subject to Division 296 tax for that year.

Further complexity arises when applying the required calculation to determine an individual's superannuation earnings – that is, determining the amount that will be subject to Division 296 tax. While at a high level an individual's superannuation earnings will be calculated based on the movement in their TSB over the course of a financial year, where there have been "contribution amounts" or "withdrawal amounts" this becomes a far more complicated proposition.

It also needs to be emphasised that this proposed new tax will only result in additional tax being levied on a proportion of an individual's superannuation earnings – that is, the proportion of their earnings that is attributable to the amount of their balance that exceeds the $3 million threshold.

In this bulletin we will aim to commence the unpacking of this proposed new Division 296 tax by highlighting some of its key features. It is not the intention of this bulletin to provide a comprehensive analysis.

It's also worth emphasising that this Bill is not yet law and may never become law. Further, if it is to become law, it is still possible that the content of this Bill may be amended as it progresses through Parliament.

At the time of writing, this Bill had been referred to the Senate Economics Legislation Committee, with its report due on the 19 April 2024.

> **NOTE**
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> **Note:** Special rules and exemptions may apply to individuals with certain types of superannuation interests and schemes. These rules and exemptions are beyond the intended scope of this bulletin at this time.
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> Nonetheless, these rules will require specific consideration where relevant to a particular individual's circumstances, as they may impact on the overall calculation of that individual's Division 296 tax liability.

Key features and observations

Introduction of new Division 296 tax

The proposed Division 296 tax will only apply from the 2025-2026 financial year onwards.

As such, the first determinations for this new tax will not be issued until sometime after 1 July 2026.

Further, there has been no suggestion that there will be any changes made to other current taxing arrangements applicable to superannuation funds as a result of this new tax. That is, for example, the 15% concessional tax rate will continue to apply to the taxable income of superannuation funds. Similarly, superannuation funds will continue to enjoy a tax exemption for eligible pension earnings.

Instead, this tax is proposed to apply in addition to the current taxing regime.

Also, much like the existing Division 293 tax, this new Division 296 tax is proposed to result in a personal tax liability – as opposed to a fund tax liability.

The cap

The proposed Division 296 tax will broadly only impact on those individuals with a TSB greater than $3 million at the end of the relevant financial year.

This threshold will not be automatically indexed and is defined in the legislation as the "large superannuation threshold".

Further, this $3 million threshold is an individual limit – that is, it is not a per fund or per couple limit.

> **Tip:** Strategies that encourage the equalisation of superannuation balances between members of a couple will likely become increasingly relevant for those individuals likely to be impacted by Division 296 tax.

Liability to Division 296 tax

The first step will be to determine whether an individual is liable for Division 296 tax for a given financial year. This will require identifying that individual's TSB at the end of the relevant financial year.

Only individuals with a TSB greater than $3 million, on 30 June of a given financial year, who have taxable superannuation earnings (discussed later) will be liable for Division 296 tax.

When determining whether an individual may be liable for Division 296 tax, the usual TSB definition applies – less any *Limited Recourse Borrowing Arrangement amounts (LRBA amounts)*.

That is, the current TSB definition includes certain LRBA amounts. Broadly, these amounts are included where:

- the member has satisfied a nil condition of release relating to retirement, terminal medical condition, permanent incapacity or attaining age 65, or
- the lender is an "associate" of the superannuation provider.

While these amounts will continue to be included in the TSB calculation to be applied for all other purposes, they will be specifically excluded from the definition of TSB that is to be used for Division 296 purposes.

NOTE

Note: With the introduction of this Bill, the Government is also proposing to amend the TSB definition. This proposed new TSB definition refers to yet-to-be released regulations. For the purposes of this bulletin, we will work on the broad assumption that the new TSB definition will include all Australian superannuation interests.

It should also be noted that certain individuals will be specifically exempted from being liable to pay Division 296 tax. These include:

- Child recipients of a superannuation income stream – for example, children in receipt of a death benefit pension e.g. following the death of a parent.
- Individuals who have, at any time, received a structured settlement contribution – that is, regardless of whether that contribution was made in the relevant year or in any earlier year.
- Individuals who died ***before*** the last day of the financial year – interestingly, if an individual were to die on the last day of the financial year (i.e. on 30 June), they would not be exempted from this new tax.

Tip: For individuals who may be considering whether to re-structure their superannuation balances to avoid incurring Division 296 tax in its ***first year*** of operation (i.e. in the 2025-26 financial year), they will need to ensure that their TSB at ***30 June 2026*** is below the $3 Million threshold. This timeframe may provide some individuals with sufficient time to consider their available options – noting of course that individuals who have not yet satisfied a condition of release will not be able to withdraw money from superannuation to avoid the tax.

Rate of tax

Once it has been established that an individual is liable for Division 296 tax, the rate of this new tax to be levied on their superannuation earnings (for Division 296 purposes) will be 15%.

However, this rate will only be applied to the proportion of an individual's superannuation earnings (for Division 296 purposes) attributable to their balance above $3 million. This proportion will be calculated by applying the following formula:

$$\frac{\text{TSB at the end of the year} - \$3{,}000{,}000}{\text{TSB at the end of the year}} \times 100$$

This formula is designed to ensure that Division 296 tax will only be applied to an individual's earnings corresponding to the percentage of their TSB that exceeds $3 million.

Superannuation earnings

The next step in determining the amount of Division 296 tax that an individual may be liable for is to determine the amount of their superannuation earnings for the relevant financial year.

When determining the amount of superannuation earnings that may be subject to Division 296 tax, an ***adjusted TSB*** definition needs to be applied.

An individual's superannuation earnings (for Division 296 tax purposes) are broadly calculated with reference to the difference in that individual's TSB at the start and end of the financial year, with adjustments made for what we will refer to as "contribution amounts" and "withdrawal amounts".

This adjusted TSB definition seeks to capture various amounts that are either added to, or removed from, an individual's superannuation balance over the course of a financial year – where those amounts do not relate to fund earnings. Without these adjustments, the magnitude of movement in an individual's TSB throughout the year could be inadvertently increased or decreased by transactions not related to earnings.

Broadly, the formula that will be used to calculate superannuation earnings is:

Current year adjusted TSB – Previous year TSB[1]

And, to determine an individual's current year adjusted TSB we will need to consider the following:

TSB at the end of the relevant year + Withdrawal total – Contributions total

NOTE

Note: Superannuation earnings (for Division 296 purposes) are measured on a year-to-year basis. That is, income and gains accrued prior to 1 July 2025 will not be subject to Division 296 tax.

Similarly, because gains are calculated on a year-to-year basis, the starting point for each financial year is the individual's TSB at the beginning of that particular financial year.

This proposed new tax will not be applied to existing superannuation balances, rather it will only be applied to the annual earnings derived thereon.

Contribution amounts

Contribution amounts include those amounts that are received into an individual's superannuation accounts throughout the relevant financial year, such as:

- Amounts contributed into the individual's superannuation fund(s) – this only includes 85% of the contribution amount where the contribution made was a concessional contribution.

[1] Where either the current year adjusted TSB, or previous year TSB, is less than $3 Million, that figure is to be substituted with $3 Million. This will be discussed later in this bulletin.

- The starting balance of a death benefit pension in the year that the death benefit pension commences, or in the case of a reversionary pension, the balance of that pension at the date of the primary pensioner's death.
- The amount of any insurance proceeds received into an individual's superannuation fund(s) as a result of death, total and permanent disability (TPD), or a terminal medical condition.
- Contributions-splitting superannuation benefits received into an individual's superannuation fund(s).
- Family law superannuation payments received into an individual's superannuation fund(s).
- Certain amounts allocated to an individual's member balance from a fund reserve.
- Certain amounts transferred from a foreign superannuation fund e.g. transfers from a QROPS fund.
- Amounts of unclaimed monies received.
- Amounts received as a result of remediation payments, or compensation for loss as a result of fraud or dishonesty.

Adjusting for these contribution amounts each year seeks to ensure that the size of the increase in an individual's TSB is not overstated due to transactions that are not linked to investment activities.

Withdrawal amounts

Perhaps not surprisingly, withdrawal amounts include amounts removed from an individual's superannuation balance during the year which would otherwise have the effect of reducing that individual's superannuation earnings (for Division 296 purposes). These amounts include:

- Superannuation member benefits e.g. lump sum withdrawals and pension payments received.
- Superannuation death benefits paid from a superannuation income stream e.g. lump sum commutations and pension payments received from a death benefit pension.
- Amounts transferred to a spouse under spouse contribution-splitting arrangements.
- Amounts transferred to another person because of a family law payment split.
- Amounts withheld from a rollover benefit, where that rollover contained untaxed element, as well as amounts paid by a receiving fund in the form of tax.
- Amounts released in response to a release authority. For example, release authorities in response to:
  - an excess concessional or excess non-concessional contributions determination,
  - a notice of assessment of an amount of Division 293 tax, or
  - a first home super saver determination.
- Amounts paid to the Commissioner during the year under the Superannuation (Unclaimed Money and Lost Members) Act 1999.

Adjusting for these withdrawal amounts each year seeks to ensure that the size of the increase in an individual's TSB is not understated, and cannot be unduly manipulated, by transactions that are not linked to investment activities.

Example:

Facts

On 30 June 2026, Holly has a TSB of $4 Million.

During the 2025-26 financial year, she made a lump sum withdrawal of $100,000 and received concessional contributions of $27,500.

Her TSB on 30 June 2025, i.e. at the start of the financial year, was $3.5 Million.

Analysis:

Step 1:	Holly's TSB at the end of the financial year will be greater than $3 Million. Therefore, if she has taxable superannuation earnings, she will be liable for Division 296 tax.
Step 2:	Calculate the ***proportion*** of Holly's superannuation earnings that will be taxable. $4,000,000 (i.e. TSB at the end of the year) – $3,000,000X 100 $4,000,000 (i.e. TSB at the end of the year) = 25.00% (rounded to 2 decimal places)
Step 3:	Calculate Holly's ***current year adjusted TSB***. $4,000,000 (i.e. TSB at end of the year) + $100,000 (i.e. withdrawal amounts) – $23,375 (i.e. 85% of concessional contribution amount) = $4,076,625
Step 4:	Calculate Holly's superannuation earnings for the 2025-26 financial year. $4,076,625 (i.e. current year adjusted TSB) – $3.5 Million (i.e. her previous year TSB) = $576,625
Step 5:	Calculate Holly's taxable superannuation earnings (apply the proportion calculated at Step 2 to her superannuation earnings calculated at Step 4). $576,625 X 25.00% = $144,156.30
Step 6:	Calculate Holly's ***Division 296 tax liability*** for the 2025-26 financial year. $144,156.30 (i.e. her taxable superannuation earnings) X 15% (i.e. Division 296 tax rate) = $21,623.44

While Holly's superannuation earnings (for Division 296 purposes) are estimated to be $576,625, only $144,156.30 of this amount will be subject to Division 296 tax – as these are the earnings that are attributable to the proportion of her superannuation balance that exceeds $3 million.

After applying the 15% Division 296 tax rate to her taxable superannuation earnings for the year, Holly's Division 296 tax liability or 2025-26 will be $21,623.44.

Initial observations

Contribution amounts

When calculating an individual's current year adjusted TSB, insurance proceeds will be specifically excluded due to the fact they will be treated as a "contribution amount" in the year they are received.

A similar outcome arises in the financial year in which a person becomes eligible to receive a death benefit pension. That is, the pension balance on the day that an individual becomes the recipient of a death benefit pension will be excluded, due to the fact it will be treated as a "contribution amount".

However, in both the above circumstances, these amounts are still included in that individual's TSB for the year – which of course is used to determine whether they may be liable for Division 296 tax for that year.

As such, if the individual's TSB at the end of the relevant financial year exceeds $3 Million, as a result of having received insurance proceeds or commenced to receive a death benefit pension, and they have taxable superannuation earnings for that year, they will now be liable to Division 296 tax – even though these amounts have been excluded as "contribution amounts".

Example:

On 1 July 2025, Craig has a TSB of $2.7 Million.

During the 2025-26 financial year, he suffers a serious injury that results in him receiving $1 Million of proceeds from his superannuation-owned insurance policy – which are paid into, and retained in, his superannuation fund.

Craig's closing TSB (i.e. on 30 June 2026) is $4.1 Million.

<u>Analysis</u>

Notwithstanding the insurance proceeds received by Craig will be excluded from the calculation of superannuation earnings in the 2025-26 financial year, Craig's TSB at the end of the 2025-26 financial year will now be greater than $3 Million.

Therefore, Craig may now be liable for Division 296 tax on any taxable superannuation earnings arising from the 2025-26 financial year.

Example:

Following Jim's death in July 2025, his wife Delilah becomes eligible to receive a death benefit pension (as his reversionary beneficiary). The balance of this pension at the date of Jim's death is $1,900,000.

On 1 July 2025, Delilah's TSB was $2.6 Million. However, on 30 June 2026, courtesy of Jim's death benefit, her TSB has now increased to $5 Million.

Example:

Following Jim's death in July 2025, his wife Delilah becomes eligible to receive a death benefit pension (as his reversionary beneficiary). The balance of this pension at the date of Jim's death is $1,900,000.

On 1 July 2025, Delilah's TSB was $2.6 Million. However, on 30 June 2026, courtesy of Jim's death benefit, her TSB has now increased to $5 Million.

<u>Analysis</u>

Even though the balance of the death benefit pension will be excluded from the calculation of Delilah's superannuation earnings in the 2025-26 financial year, her TSB at the end of the 2025-26 financial year will now be greater than $3 Million[1].

Therefore, Delilah may now be liable for Division 296 tax on any taxable superannuation earnings arising in the 2025-26 financial year.

Withdrawal amounts

As illustrated by the above discussion, amounts withdrawn from an individual's superannuation balance during the year will be added back when calculating that individual's *current year adjusted TSB* – they will therefore be included in their superannuation earnings for that year.

As such, on the surface at least, it may appear that withdrawals will not assist with reducing an individual's Division 296 tax liability for a given year – that is, the withdrawal amount will be included in the calculation of their superannuation earnings for the year.

However, as a withdrawal will typically result in a reduction to that individual's TSB at the end of the year, by having a lower closing TSB the proportion of superannuation earnings that will be subject to Division 296 tax will be reduced.

Further, where an individual's TSB at the end of the year is reduced to below $3 Million, Division 296 tax will be avoided altogether – that is, they will no longer be liable for Division 296 tax as their TSB is below the $3 Million large superannuation threshold.

Example:

Let's consider Holly from our earlier example. However, let's now assume that she made an additional lump sum withdrawal of $250,000 on 30 June 2026.

As a result of this commutation her TSB on 30 June 2026 is now $3.75 Million (from $4 Million previously).

<u>Analysis</u>

Holly will still be subject to Division 296 tax as her TSB is greater than $3 Million.

The amount of her superannuation earnings for the financial year will also remain unchanged, as the additional amount withdrawn will also be added back as a "withdrawal amount".

However, when calculating the proportion of Holly's superannuation earnings that will be taxable, we now see that:

Step 2:	Calculate the proportion of Holly's superannuation earnings that will be taxable. <u>$***3.75 Million*** (i.e. TSB at the end of the year) – $3,000,000</u> X 100 $***3.75 Million*** (i.e. TSB at the end of the year) ***= 20.00% (rounded to 2 decimal places)***

As a result of the additional withdrawal made by Holly on 30 June 2026, the proportion of her superannuation earnings that will be subject to Division 296 tax will reduce from 25.00% to 20.00%, her taxable superannuation earnings will reduce from $144,156.30 to $115,325, and therefore her Division 296 tax liability will reduce from $21,623.44 to $17,298.75.

Unrealised investment gains

After allowing for the abovementioned adjustments to an individual's TSB – i.e. in determining their current year adjusted TSB, this proposed new tax will broadly capture annual movements in a member's TSB due to movements in that member's superannuation investments, as superannuation earnings.

Due to this feature in the design of this new tax, i.e. only tracking investment-related movements in a member's balance, this measure is unable to make any distinction between realised or unrealised investment returns – resulting in Division 296 tax potentially being payable on a member's unrealised superannuation gains.

Moving in (or out) of the Division 296 Realm

As already discussed earlier in this bulletin, an individual's superannuation earnings (for Division 296 purposes) are broadly determined by calculating the divergence between an individual's previous year TSB and their current year adjusted TSB.

However, an additional tweak to the calculation is required where an individual moves into, or out of, the Division 296 realm during a financial year.

That is, where either an individual's current year adjusted TSB, or previous year TSB, is less than $3 Million the calculation varies slightly. Where this phenomenon occurs, the offending figure is to be substituted with $3 Million.

Example:

Let's consider Delilah from our previous example.

On 1 July 2025, Delilah's TSB was $2.6 Million. However, on 30 June 2026, courtesy of Jim's death benefit, her TSB has increased to $5 Million.

We've already established that her TSB at the end of the 2025-26 financial year now exceeds $3 Million and she may therefore be subject to Division 296 tax in that year.

However, as her previous year TSB was less than $3 Million (i.e. $2.6 Million), when applying the formula to calculate her superannuation earnings for Division 296 tax purposes, we need to substitute her previous year TSB of $2.6 Million with $3 Million, as follows:

Delilah's current year adjusted TSB will be:

$5 Million (i.e. TSB at end of the year) – $1,900,000 (i.e. contribution amounts)

= $3,100,000

Delilah's superannuation earnings for the 2025-26 financial year will be calculated as:

$3,100,000 (i.e. current year adjusted TSB) – ***$3 Million (i.e. substituted previous year TSB)***

= $100,000

This results in a lower superannuation earnings figure for Delilah. That is, if her previous year TSB of $2.6 Million had been used, her superannuation earnings for 2025-26 would have been $500.000.

This also applies where the opposite occurs. That is, if an individual's previous year TSB was greater than $3 Million, meaning they were previously subject to Division 296 tax, but their current year adjusted TSB has fallen to be below $3 Million, when calculating the amount of *negative earnings* that can be carried forward, the member's current year adjusted TSB in the formula must similarly be substituted with $3 Million.

Example:

On 30 June 2026, Gladys has a TSB of $3.4 Million.

Due to some poor investment decisions, her TSB on 30 June 2027 falls to $2.8 Million.
There are no "contribution amounts" or "withdrawal amounts". Clearly Gladys has experienced an overall negative return in the 2026-27 financial year.

When calculating Gladys' superannuation earnings, which will determine the amount that may be carried forward for future use, we are required to substitute her current year adjusted TSB of $2.8 Million with $3 Million. As such, Gladys' earnings for 2026-27 will be:

$3 Million (i.e. substituted for current year adjusted TSB) – $3.4 Million (previous year TSB)

= ($400,000)

Even though she has experienced a reduction of $600,000 to her TSB over the year, for Division 296 tax purposes her negative earnings will only reflect a $400,000 loss.

Negative earnings

At the risk of oversimplifying the aspects of this legislation that deal with negative earnings, where an individual's superannuation earnings are less than nil for a given financial year, the amount of these negative earnings may be carried forward to reduce their superannuation earnings in future years. These amounts are broadly referred to as transferable negative superannuation earnings.

Where an individual has ***unapplied*** transferrable negative superannuation earnings for a given financial year, i.e. negative earning amounts carried forward from an earlier year, their superannuation earnings for a subsequent year in which they are subject to Division 296 tax will be reduced by applying their unapplied transferrable negative superannuation earnings.

That is, superannuation earnings for a financial year will typically be reduced by losses carried forward from previous years.

This calculation will essentially involve subtracting an individual's unapplied transferrable negative superannuation earnings from their superannuation earnings.

Example:

Let's re-visit Gladys from our earlier example.

We previously established that Gladys's superannuation earnings for the 2026-27 financial year are estimated to be ($400,000). That is, she will experience negative superannuation earnings.

Let's now assume that on 30 June 2028, Gladys' TSB has risen to $3.5 Million due to strong investment growth – and for the sake of simplicity, let's assume there were no "contribution amounts" or "withdrawal amounts" during the year.

<u>Analysis</u>

Gladys may now be subject to Division 296 tax as her TSB is greater than $3 Million.

To calculate Gladys' superannuation earnings for the 2027-28 financial year, we are required to substitute her *previous year TSB* with $3 Million (as her actual TSB on 30 June 2027 was $2.8 Million).

Her *current year adjusted TSB* is $3.5 Million.

Therefore, Gladys' superannuation earnings for 2027-28 will be:

$3.5 Million (i.e. current year adjusted TSB) – $3 Million (substituted previous year TSB)

= $500,000

However, as her superannuation earnings for the 2026-27 financial year were less than nil, Gladys has $400,000 of unapplied transferrable negative superannuation earnings from the 2026-27 financial year.

As a result, once we subtract this amount from the $500,000 of earnings calculated above, Gladys' superannuation earnings for the 2027-28 financial year are reduced to $100,000.

Paying the tax liability

Much like Division 293 tax, any Division 296 tax liability that arises rests with the individual taxpayer. That is, it's the taxpayer who must foot the bill.

To that end, where an individual is liable for Division 296 tax, the ATO Commissioner will generally issue them with a notice of assessment for the tax. And the individual will generally be required to pay the tax liability within 84 days of the Commissioner giving them the notice of assessment.

However, individuals can choose how they pay their Division 296 tax liability. That is, they will have the option of paying their tax liability either by releasing amounts from one (or more) of their superannuation interests, by paying the liability from outside of the superannuation system (i.e. using personal or other available funds), or a combination of the two. This will be the case irrespective of whether they have met a condition of release.

Where an individual intends to have an amount released from a superannuation interest, they will have 60 days of the notice of assessment, to make an election for an amount to be released from one or more of their superannuation funds (without incurring interest).

Individual with multiple superannuation interests will also be able to choose which interest(s) to release the money from.

If some or all of the Division 296 tax is not paid within the required 84-day period, the Commissioner may issue a release authority to one or more superannuation providers that holds a superannuation interest for the individual.

Failure to pay the liability within the required timeframe may result in the application of additional interest charges.

NOTE

Note: The period of 84 days is longer than the payment window for similar forms of tax, such as Division 293 tax. This is to allow additional time for individuals with less predictable sources of income to make arrangements to pay the tax liability.

Closing thoughts

As noted at the start of this bulletin, this new Division 296 tax is not yet law, may not become law, and even if it does become law, may vary from its current form – which we have sought to summarise in this bulletin.

However, with the Bill currently being scrutinised by a Senate Committee, and as it inches closer to becoming law, in the midst of ongoing advocacy efforts for the proposed tax to be scrapped or at least modified, it is important to begin to understand how it is intended to operate, in its current form, to be able to better assist clients who may be impacted by this new tax.

We have intentionally omitted any discussion on special rules and exemptions that may apply to certain superannuation interests to avoid unnecessarily distracting from the key features of this proposed new tax. Even so, as evidenced in this bulletin, there is still a great deal of complexity to be considered for those who may be impacted.

CPD quiz

Please click here to access the CPD quiz.

If you have difficulties accessing the quiz via the above link, please copy and paste this URL into a new browser: http://web.smsfassociation.com/smsfassociationcom-ah3t2/pages/44330edc5399ee11be3700224894af01.html?PageId=44330edc5399ee11be3700224894af01