Federal Budget Update

May 2010

Key highlights

- Discounted tax treatment for first $1,000 of interest earned on deposits
- Changes to deductible rate for capital protected borrowings
- Standard deduction for work-related expenses to simplify tax return process
- Restatement of measures announced in response to Henry Tax Review

Overview

On 11 May 2010, the Federal Government handed down its Budget for 2010/11.

From a financial planning perspective, a “sound”, well-formed personal budget has few surprises. Perhaps, in this year’s Federal Budget, this is what the Government has delivered.

There was little in the way of pre-election sweeteners, other than some concessional tax treatment for certain non-super investments and proposed simplification of the tax return process through standard deductions being available for most working Australians. These changes however will not come into effect until after the next election, indicating that they would form part of the Government’s election plans.

The sweetener may actually be in the lack of “benefits”. With a greater emphasis on saving and by not continuing with the fiscal stimulus levels of previous years, there may be a reduced need for future interest rate rises – something that would actually benefit many Australians.

Certainly, there were no major surprises, with many of the major changes being announced in the Government’s response on 2 May 2010 to Australia’s Future Tax System (commonly referred to as the Henry Tax Review). It must also be noted that most measures will still need legislation to be introduced, so the final version of the changes may differ to the announcements made in the Budget.

As with all changes, it is important that you speak with your financial adviser to determine how these announcements will impact your personal situation.

Taxation

Changes to personal tax rates

Effective date: 1 July 2010

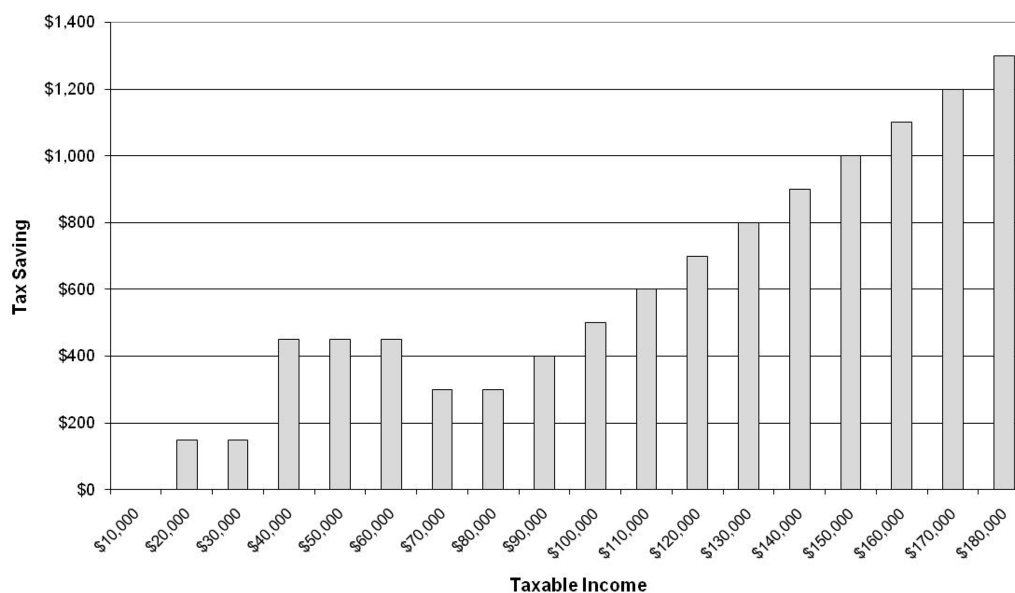
From 1 July 2010, personal income tax changes will come into effect. These changes were announced in 2008 and no further adjustments have been made.

Current		From 1 July 2010	
Taxable income	**Rate**	**Taxable income**	**Rate**
0- $6,000	0%	0- $6,000	0%
$6,001 - $35,000	15%	$6,001 - $37,000	15%
$35,001 - $80,000	30%	$37,001 - $80,000	30%
$80,001 - $180,000	38%	$80,001 - $180,000	37%
$180,001+	45%	$180,001+	45%

The Low Income Tax Offset will increase from $1,350 to $1,500 for 2010/11, phasing out after $30,000 by 0.04 cents in the dollar to a maximum of $67,500.

The graph below shows the tax savings for the 2010/11 financial year as compared to the 2009/10 financial year.

Tax Saving from 2010/11 Budget



As a result of these changes, from 1 July 2010 if your taxable income doesn't exceed $16,000 you will have no tax to pay. If your taxable income is up to $30,000, you will effectively receive the first $16,000 tax free and only pay 16.5% tax on the balance.

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Increase in the Medicare levy low income thresholds

Effective date: 1 July 2009

The Government has announced new Medicare levy thresholds that are applicable for the current financial year (ending 30 June 2010). These are $18,488 for individuals (previously $17,794) and $31,196 for families (previously $30,025). The increase on these thresholds for each dependent child or student will be $2,865. If your taxable income is below these levels, you will not have to pay the 1.5% Medicare levy.

The low income threshold for pensioners below the age pension age has been increased to $27,697 for the year ending 30 June 2010. This will ensure such pensioners do not pay the Medicare levy when they do not have an income tax liability.

Increase in the net medical expense tax offset claim threshold

Effective date: 1 July 2010

The Government has announced an increase in the threshold above which you can claim the 20% net medical expense tax offset. From 1 July 2010 the threshold will rise from $1,500 to $2,000. In addition, this threshold will be indexed annually to the Consumer Price Index.

Standard rate of tax deductions to simplify tax returns

Effective date: From 1 July 2012

From 1 July 2012, individual taxpayers will have the option of receiving a standard deduction of $500 for work related expenses and the cost of managing tax affairs. From 1 July 2013, the Government will increase this standard deduction to $1,000. If your deductible expenses are greater than the standard deduction amount, you will be able to claim the higher expenses when lodging your tax return under the existing rules, but will need to substantiate the higher claim.

The Government expects that for many this will lead to a 'tick and flick' system of pre-filled tax returns and reduce the reliance and cost of using tax agents to complete simple tax returns.

Discounted assessability on first $1,000 of interest income

Effective date: 1 July 2011

From 1 July, 2011 the Government will provide individuals a 50% tax discount on up to $1,000 of interest earned from a range of savings products. The savings products attracting the concessions include bonds, debentures or annuity products as well as deposits held with a bank, building society or credit union.

Examples

- On 1 July, 2011 Jack deposits $10,000 in a one-year term deposit with an effective rate of 5% per annum, earning $500 after one year. Jack would be required to include only $250 of this interest income in his tax return.
- On 1 July, 2011 Jill deposited $40,000 in a one-year term deposit with an effective rate of 5% per annum, earning $2,000 after one year. Jill would be required to include only $1,500 of this interest income in her tax return.

Changes to company tax

Effective date: From 1 July 2012 for small business companies, otherwise from 1 July 2013

As detailed in its response to the Henry Tax Review, the Government has announced that the company tax rate will be gradually reduced from its current 30% level to 28% in accordance with the following timeline:

Income year	Rate for small business companies	Rates for other companies
Up to and including 2011/12	30%	30%
2012/13	28%	30%
2013/14	28%	29%
2014/15 and later years	28%	28%

For investors, the reduction in company tax rates will have an impact on the tax effectiveness of franked dividends, meaning they will either have to pay additional tax on franked distributions or suffer a reduction in any excess imputation credits that would otherwise have been refunded. However, the reduction in company tax may mean these companies could pay a higher level of dividend in future years.

Small business tax relief

Effective date: 1 July 2012

Currently small businesses (those with annual turnover of under $2 million or net assets less than $6 million) can immediately write-off expenses for assets worth up to $1,000 in value. From 1 July 2012, small businesses will be able to immediately write-off assets which have a value of less than $5,000.

Additionally, small businesses will be able to have one depreciation pool for all other assets (excluding buildings) and write-off this pool of assets at 30%. Currently, they allocate assets to two different depreciation pools.

This will:
- simplify depreciation calculations and reduce compliance costs by removing the requirement to calculate depreciation allowances and track assets for depreciation
- increase their cash-flow by deferring tax liabilities
- make asset ownership more attractive than leasing or debt financing.

Income tax treatment of instalment warrants

Effective date: 1 July 2007

Consistent with a pre-budget announcement, the Government intends to amend the taxation law surrounding instalment warrants to ensure that for capital gains tax purposes the owner of an instalment warrant over an exchange traded security will be treated as the owner of the security.

The amendments will provide certainty that a capital gains tax event will not be realised once the legal ownership of the asset is transferred to the investor. The capital gains tax event will happen on the disposal of the trust asset. The disposal of the instalment warrant will be treated as a disposal of the trust.

This treatment will also apply to instalment arrangements within superannuation funds under the 2007 amendments that allow gearing within superannuation.

Change to Benchmark Interest Rate for Capital Protected Borrowing

Effective date: 13 May 2008

The ‘benchmark interest rate’ that applies to capital protected borrowings will be adjusted to the Reserve Bank of Australia (RBA) indicator rate for standard variable housing loans plus 1%. The measure will apply to capital protected borrowings entered into at, or after, 7:30pm (AEST) on 13 May 2008.

Where the capital protected component of the interest charged on a capital protected arrangement is not specified, the amount in excess of the benchmark interest rate is treated as the capital protection component of the interest and is not deductible. This excess amount is however capital in nature and should be able to be added to the cost base of the asset. The relevant benchmark interest rate at April 2010 would be 8.15%.

Capital Gains Tax (CGT) look-through provision for earn out payments

Effective date: generally from date of Royal Assent

Under some business sale arrangements, clauses are contained in the sale documentation that effectively allow for additional payments to be made between the buyer and seller based on the performance of the business post sale.

Current CGT legislation can result in a situation where more tax is payable than would otherwise be applicable if those payments formed part of the initial sale price as the right to these payments is considered a separate asset for CGT purposes. The Government will legislate to remove this anomaly.

Superannuation

Restatement of measures announced in response to Henry Tax review

Effective date: 1 July 2012 or later

The Budget contained a restatement of four main changes to superannuation announced on 2 May 2010 as part of the Government's response to the Henry Tax Review, being:

- **An increase in the superannuation guarantee rate from 9% to 12% by 2019/20.**

  The superannuation guarantee (SG) rate will be increased from 9% to 12% over a seven year period, commencing from 1 July 2013, with the increased rate of 12% applicable from 1 July 2019, as per the following table:

Year	SG rate
2013/14	9.25%
2014/15	9.50%
2015/16	10.00%
2016/17	10.50%
2017/18	11.00%
2018/19	11.50%
2019/20	12.00%

  On a salary of $50,000, the additional 3% SG contribution will add an extra $1,500 per annum to superannuation (before tax). If that contribution were to earn 7% per annum (net of fees and taxes), its value would double every 10 years.

  It will be important to understand how your employer decides to fund this increase as current legislation allows employers to deduct this from your overall package (this may be different under some award arrangements).

  For an employee on $50,000 per annum, the extra $1,500 super contribution will provide $1,275 in super after tax per annum, against a take home after tax amount of $923 if that had continued to be received as salary. The extra super contribution delivers an extra 38% value.

- **A low income earner government super contribution of up to $500**

  From 1 July 2012, low income earners will be entitled to an additional government contribution into their superannuation fund of up to $500. This is in addition to any government co-contribution payment you may be entitled to.

  The payment is available if your adjusted taxable income is $37,000 or less, with the amount of the contribution being equal to the contributions tax that would be payable on your compulsory SG contributions.

  For example, a person with a salary of $37,000 would have compulsory SG contributions of $3,300 made for the year ended 30 June 2013. Standard tax on those contributions (at 15%) amounts to $499.50 so the individual would receive the maximum benefit from the contribution. For a person earning a salary of $25,000 the contribution would amount to $337.50 (being $25,000 x 9% x 15%).

- **A permanent extension of the current transitional concessional contributions cap of $50,000 for those aged 50 and over if their superannuation balance is below $500,000.**

  The transitional concessional contributions cap of $50,000 for those aged 50 and over will no longer cease on 30 June 2012, but instead will become a permanent measure.

However, this will only be available from 1 July 2012 if your total superannuation balance is below $500,000. The concessional contributions cap applies to contributions for which a tax deduction is available, such as SG payments, salary sacrificed amounts and personal deducted contributions to super.

Opportunities may arise to maximise advantage of this extended concession through appropriate use of transition to retirement and contribution strategies and through careful management of the timing of contributions. You should discuss these opportunities with your adviser.

- **Raising the superannuation guarantee age limit from 70 to 75.**

  In a move designed as an incentive to keep people working for longer, the age limit at which an employer's requirement to make SG contributions for employees ceases will be lifted from 70 to 75. This change will have effect from 1 July 2013, coinciding with the increased rate of SG contributions.

Changes to government co-contribution

Effective date: 1 July 2010

In last year's Budget the Government announced a temporary reduction in the matching rate for the government superannuation co-contribution measure. This reduction has now been made permanent, such that co-contributions will now only be available on a 1:1 matching basis to a maximum co-contribution level of $1,000.

In addition the current thresholds applying for co-contribution eligibility will be frozen for the next two years, rather than being indexed on 1 July. For 2010/11 and 2011/12, the maximum co-contribution will only be available if your income level doesn't exceed $31,920, and no co-contribution will be available once your qualifying level of income reaches $61,920.

No minimum pension reduction extended

Effective date: Not applicable

For 2008/09 and 2009/10, the minimum payment required out of superannuation pensions was halved in recognition of the impact of the global financial crisis. This temporary reduction will not apply for the 2010/11 income year.

Additional ATO discretion on excess superannuation contribution tax assessments

Effective date: intended to apply from 1 July 2010

The Government announced that the Commissioner of Taxation will be allowed to exercise discretion for the purpose of excess contribution tax before an assessment is issued.

The current arrangements provide very little discretion for the Commissioner to exercise discretion in relation to excess contribution tax amounts even where you have made a genuine mistake and unintentionally breached the superannuation contribution caps.

With over 35,000 taxpayers having breached the contribution caps in the 2008/09 financial year, excess contribution tax has become an issue for a substantial number of individuals. Depending on the detail of the announcement, this measure will hopefully provide the Commissioner with sufficient additional powers to exercise discretion prior to an assessment being made where the contribution caps have inadvertently been breached.

Other

Increasing Flexibility in First Home Saver Accounts

Effective date: Royal Assent of Supporting Legislation

Balances in first home saver accounts (FHSAs) will be allowed to be paid into an approved mortgage after the end of the minimum qualifying period rather than requiring it to be paid to a superannuation account. Under the current rules, deposits must be held in FHSAs for four financial years before they are able to use those savings to buy a home. If the account holder buys a home prior to the end of the four year period, the balance of the account had to be transferred to the holder's superannuation fund.

The changes mean that individuals who choose to purchase a home before the end of the four year qualification period will be able to pay any accumulated balance in their FHSA into an approved mortgage at the end of the qualification period.

To qualify under the current rules, individuals either have to attain age 60 or meet the 4 year rule and the meet requirements as follows.

- Occupancy Rule – must be a main residence for at least 6 months after date of acquisition;
- 4 Year Rule – must have 4 qualifying years where at least $1,000 pa is contributed to the FHSA. If the $75,000 balance limit is breached, no contributions can be made and they must hold the account for at least 4 years.

The change should provide greater confidence for those who are saving for their first homes to invest using a FHSA and gain the tax benefits associated with doing so.

Paid Parental Leave

Effective date: 1 January 2011

The Paid Parental Leave (PPL) scheme was announced in the May 2009 Budget. The scheme will provide a new parent of a child born or adopted from 1 January 2011 a payment equivalent to the national minimum wage for 18 weeks. The payments (current rate is $543.78 pw) will be made through the parent's employer. To be eligible the parent must:

- be working for 10 out of 13 months before the birth or adoption of the child
- have at least 330 hours paid work in the 10 month period
- have an adjusted taxable income up to $150,000 in the previous financial year.

The scheme is available to employees, casual workers, contractors and self-employed individuals. PPL can be claimed as an alternative to the Baby Bonus (except for multiple births). Family Tax Benefit B will not be paid for an 18 month period. Total PPL ($9,788.04) will be more generous than the Baby Bonus ($5,185) and FTB B ($3,828.85) combined. Dependent spouse, child, and housekeeper tax offsets will not be available for the PPL period.

Special Disability Trusts

Effective date: 1 July 2011

Special Disability Trusts enable parents and immediate family members to put money aside for the future care and accommodation needs of a family member with a severe disability.

Whilst the concessions have been generous, the take up has been limited because of the restrictions placed on the access and use of the funds and the necessary level of disability. The Government has announced the following changes.

- The definition of beneficiary will expand to include people capable of working up to 7 hours per week (excluding work in an Australian Disability Enterprise).
- Allowable uses of trust funds will be expanded to include all medical expenses and private health insurance, maintenance of the principle residence if owned by the trust and discretionary spending of up to $10,000 per year.

These changes may make the trusts a more attractive proposition.

Family Tax Benefit Part A

Effective date: 1 July 2010

If a parent qualifies for Family Tax Benefit Part A, a child aged between 16 and 20 who does not have a Year 12 or equivalent qualification must participate in full time education or training. It had previously been announced that a combination of education or training and other approved activities would be acceptable.

Youth Allowance will remain an option for children in this age group.

Disclaimer
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