Aspects of Financial Planning

Federal Budget 2010

May 2010

Background

On 11 May 2010, the Treasurer, the Hon. Wayne Swan MP, delivered his third Federal Budget.

Mr Swan said that the Budget's main focus was a move from supporting the economy through the economic slowdown to bringing Australia back into surplus. This shift would produce an economic and fiscal position that would be the envy of the developed world, with a stronger, more secure future for Australians.

An underlying cash deficit of over $40 billion was estimated for 2010/11 with a return to surplus brought forward from the previously projected 2015/16 to 2012/13. Government debt is estimated to peak at over $93 billion in 2012/13.

The 2010 Federal Budget was preceded by the Government's response to the 'Henry Tax Review' on 2 May 2010 which provided the majority of the measures within the Budget.

The linchpin of the Government's response to the Henry Tax Review and the Budget was the announcement of a Resource Super Profits tax (RSPT) commencing from 1 July 2012. The RSPT will be payable at a rate of 40% on the profits attributable to non-renewable resource deposits. Many of the announcements in the Budget are funded by the RSPT.

Our primary concern is the immediate and practical effect both the Government's response to the Henry Review and the Federal Budget will have on Centric Wealth clients. The following areas are those which may be of significant interest to our clients.

Personal taxation

Tax threshold and rate changes

On a positive note for all taxpayers the previously legislated taxation cuts due to commence on 1 July 2010 have not been altered by the Budget. The tax thresholds and rates applicable from 1 July 2010 are provided in the table below. Note that the highlighted figures represent the changes between this financial year and next.

2009/10		2010/11	
Tax Thresholds	Tax Rates	Tax Thresholds	Tax Rates
$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%

As was the case last year, changes to tax thresholds and rates may affect existing salary sacrifice, transition to retirement and/or margin lending strategies. More disposable income can assist to increase your wealth accumulation strategies and it is worthwhile reviewing your position in light of the threshold and tax rate changes.

Low income tax offset (LITO) and Senior Australians Tax Offset (SATO)

Similarly, changes to the LITO and SATO that have already been legislated have been left intact.

The LITO will increase from $1,350 to $1,500 from 1 July 2010. This will provide tax free income for those whose taxable income is less than $16,000.

From 1 July 2010 senior Australians entitled to the SATO will have no income tax liability until their income reaches $30,685 for singles and $26,680 for each member of a couple.

Medicare levy thresholds increased

The Government has announced the annual increased level of income that a taxpayer can earn without having to pay the Medicare levy. These revised thresholds apply for the 2009/10 financial year and are:

- $18,488 for singles; and
- $31,196, plus $2,865 for each dependent child or student, for families.

In addition, the threshold for pensioners who are below Age Pension age will be increased to $27,697 ensuring that no Medicare levy is payable when these pensioners do not have an income tax liability in a financial year.

Net medical expenses tax offset

The net medical expenses tax offset allows an individual to be reimbursed for some out of pocket medical expenses in a financial year. Currently, the tax offset is 20% of net medical expenses that exceed the threshold of $1,500. This offset is not means tested.

The Government has announced an increase to the threshold from $1,500 to $2,000 with effect from 1 July 2010. In addition, this threshold would commence to be indexed annually from 1 July 2011. An increase in the threshold means less offset is available to individuals.

50% discount for interest income

A measure that previously had not been announced is that from 1 July 2011, the Government will provide a 50% tax discount on up to $1,000 of interest earned by individuals, including through trusts or managed investment schemes. This will apply to interest earned on deposits in bank accounts, building societies, credit unions and savings held through bonds, debentures and annuities.

The table below illustrates the tax saving on $1,000 of interest income:

Tax thresholds – 2010/11	Tax rates	Tax savings
$0 - $6,000	0%	$0
$6,001 - $37,000	15%	$75
$37,001 - $80,000	30%	$150
$80,001 - $180,000	37%	$185
$180,001 +	45%	$225

The Government has stated that it will consult during 2010/11 on the operation of the discount, including the scope of the discount and the mechanism for applying the discount to interest earned indirectly by individuals.

An added benefit of the 50% discount means individuals and families will have a reduced adjusted taxable income for the purpose of determining eligibility for the Family Tax Benefits and others such as the Baby Bonus, Child Care Benefit, Education Tax Refund, Commonwealth Seniors Health Card (CSHC) and the Seniors Supplement.

Most people who have some form of bank account savings should benefit from the discount, however we don't envisage any significant change in a person's investment strategy because of the measure.

Standard deduction for work related expenses and the cost of managing tax affairs

As recommended in the Henry Tax Review, the Government will provide individuals with a standard tax deduction for work related expenses and the cost of managing their tax affairs.

From 1 July 2012, the standard deduction will be $500 increasing to $1,000 from 1 July 2013.

However, individuals who may have tax deductible work related expenses greater than the standard deduction amount will still be able to claim their higher expenses in lieu of claiming the standard deduction.

As with the interest discount, the standard deduction will reduce adjusted taxable income for individuals and families when determining their eligibility for other benefits as listed above.

This measure may benefit people whose work related expenses and costs for managing their tax affairs are below the standard deduction amounts potentially increasing their tax refunds.

Company tax

Reduction in the company tax rate

As announced in the Government's response to the Henry Tax Review, the Government will reduce the company tax rate from 30% as follows:

Year	Small business company*	Other company
2012/13	28%	30%
2013/14	28%	29%
2014/15	28%	28%

*A company with turnover less than $2 million.

Apart from companies paying less tax, this measure may result in shareholders receiving higher cash dividends but smaller imputation credits.

Investors in Australian shares (either directly or through managed funds) may find that in 2013/14 they receive a larger dividend or cash distribution reflecting the reduced 29% tax payable by companies. Further, they may receive the benefit of the 30% imputation credit from the previous financial year through their tax return. This should also be the case in 2014/15 with the tax rate decreasing to 28% combined with a 29% imputation credit.

Superannuation

As with most of the Federal Budget, the majority of the announcements concerning superannuation were pre-empted in the Government's response to the Henry Tax Review. However, one area of superannuation that was not part of the Government's response to this review but was announced in the Budget was further changes to the Government co-contribution. All of the proposed changes to superannuation are discussed below.

Contribution rebate for low income earners

From 1 July 2012, the Government will provide a superannuation contributions tax rebate to superannuation fund member's accounts where adjusted taxable incomes (ATI) are less than $37,000.

The superannuation contributions rebate would be a maximum of $500 paid annually and represents a refund of the tax payable by superannuation funds on concessional contributions.

The $500 rebate is effectively calculated by:
$37,000 x 9% x 15% = $500.

Where:

- 9% reflects the compulsory superannuation guarantee (SG); and
- 15% reflects the complying superannuation fund tax rate.

In reality, as most superannuation funds effectively pay less than 15% tax due to allowable tax deductions, members who qualify for the rebate may find a greater amount rebated than tax deducted from their benefit by their superannuation fund.

The Government will consult on the details of these changes.

The contribution rebate ensures that those with ATI less than $37,000 who are paying less than 15% tax on their incomes are not disadvantaged by the tax paid by superannuation funds on concessional contributions.

Increasing concessional contribution cap

Individuals aged 50 and over who have superannuation balances of less than $500,000 will be able to continue making concessional superannuation contributions up to $50,000 without exceeding the concessional contribution cap from 1 July 2012.

For those individuals aged 50 and over whose superannuation balances are greater than $500,000, their caps will revert to $25,000 (indexed).

Even though this measure is proposed to commence on 1 July 2012, it is important for those whose superannuation balance is approaching or has just exceeded $500,000 to start considering now what they need to do to take advantage of the higher concessional contribution cap.

Strategies that could be used to manage this include:

- Reviewing or commencing a transition to retirement income stream
- Contribution splitting with your spouse; and
- Using reserves for 'return smoothing' in self managed superannuation funds.

These strategies may be especially beneficial for a couple where one member has a significantly lower superannuation balance than the other. Your Centric Wealth adviser is able to discuss these strategies with you.

In the Government's response to the Henry Tax Review, the Government said they would consult further on the operation of the $500,000 balance. For example it is unclear at this stage whether pension balances will be included in the $500,000 figure.

Increase to superannuation guarantee to 12%

The Government will increase the superannuation guarantee (SG) rate from 9% to 12% as announced in their response to the Henry Tax Review.

The increase will be phased in from 1 July 2013 to 1 July 2019, as shown in the table below.

Year	Rate (%)
2013/14	9.25
2014/15	9.5
2015/16	10
2016/17	10.5
2017/18	11
2018/19	11.5
2019/20	12

High income earners, who may be salary sacrificing to superannuation, would need to regularly monitor their employers' SG contributions and salary sacrifice arrangements to avoid breaching their concessional contributions cap as the SG rate rises.

Extending superannuation guarantee to age 75

As announced in the Government's response to the Henry Tax Review, the Government will raise the superannuation guarantee (SG) age limit from 70 to 75 with effect from 1 July 2013.

From 1 July 2013, those aged 70 to 75 who are making personal concessional contributions or are salary sacrificing to superannuation should review their contribution arrangements to avoid breaching the concessional contribution cap.

Changes to co-contributions

In the 2008 Federal Budget, the Government announced and subsequently enacted a temporary reduction in the matching rate and the maximum co-contribution until 1 July 2014 when the co-contribution would return to the previous rate and amount.

However, in this Budget the Government announced it will be permanently retaining the matching rate for the co-contribution at 100% with the maximum co-contribution payable of $1,000. (This was due to revert back to a 150% matching rate and a maximum co-contribution of $1,500).

In addition, the Government announced that it will freeze the income thresholds at which people qualify for the full or part co-contribution for the next two financial years. The threshold to qualify for the maximum co-contribution will be frozen at $31,920 and will continue to phase out for those with incomes of up to $61,920.

This is a disappointing development for the co-contribution scheme which is no longer as generous as it was prior to the 2008 Federal Budget. However, it does not diminish the benefit for those whose income is less than $31,920 who make a non-concessional contribution and in turn receive the maximum co-contribution benefit.

Tax deductions for superannuation funds for cost of terminal medical conditions benefits

Superannuation funds, including self managed superannuation funds, will be able to claim a tax deduction for the cost of providing terminal medical condition (TMC) benefits.

The Government proposed this will take effect from 16 February 2008 when TMC first became a condition of release.

This brings the TMC condition of release in line with the death, permanent incapacity and temporary incapacity conditions of release in terms of being a tax deductible benefit provided by the fund.

Other superannuation

The Government announced it will make a number of minor amendments to improve the operation of the superannuation system that will take effect from the 2010/11 financial year.

The amendments will include:

- Increasing the time limit for deductible employer contributions made for former employees
- Clarifying the due date of the shortfall interest charge for the purposes of excess contributions tax; and
- Allowing the Commissioner of Taxation to exercise discretion for the purposes of excess contributions tax before an assessment is issued.

Other changes

There are many other smaller changes that may affect our clients. These include, but are not limited to the following:

Changes to the benchmark interest rate for capital protected borrowings

In the 2008 Federal Budget the Government announced changes to capital protected borrowing arrangements. These have yet to be legislated.
In the 2010 Federal Budget, the Government announced it will adjust the benchmark interest rate that applies to capital protected borrowings as previously announced in the 2008 Budget.

The measure will apply to capital protected borrowings entered into from 7:30 pm (AEST) 13 May 2008.

In addition, the Government will also extend the transitional arrangements for capital protected borrowings entered into at or before 7:30 pm (AEST) 13 May 2008 from the announced 13 May 2013 to 30 June 2013.

Income tax treatment of instalment warrants

The Government will amend the income tax treatment of qualifying instalment warrants by treating the investor as the owner of the underlying asset for income tax purposes with effect from 1 July 2007.

This measure was previously announced by the Minister for Financial Services, Superannuation and Corporate Law and the Assistant Treasurer on 10 March 2010. This is beneficial for clients with self managed superannuation funds (SMSFs) who are looking to borrow through their SMSFs in order to fund the acquisition of assets.

Greater accessibility for special disability trusts

The Government announced changes that will expand the definition of a beneficiary to include people with a disability who can work up to seven hours per week excluding work in an Australian Disability Enterprise.

In addition, the Government announced that it will amend the allowable uses to include all medical expenses, membership costs of private health funds, maintenance expenses of special disability trust property and discretionary spending of up to $10,000 per year.

Centric Wealth Advisers Ltd may be able to be of assistance

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