Meridian e-news

Meridian Financial Group

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Introduction

Federal Treasurer Wayne Swan has handed down his third Budget promising to return the Budget to surplus in three years.

The fiscally conservative Budget reconfirmed the recent announcements by Treasurer Swan in response to the Henry Tax Review

In addition there were a number of changes to taxation, superannuation and social security benefits.

These changes include lower tax on bank savings with a 50 per cent discount on up to $1000 of interest income, standard deductions for tax returns and childcare rebate capped to 2008-09 level of $7500 per child.

This Budget Briefing provides a summary of the relevant budget annoucements and how they may affect you.

Taxation

50% savings discount for interest income from 1 July 2011

The Government plans to provide a 50% tax discount on up to $1,000 of interest earned by individuals, including interest earned on deposits held in authorised deposit taking institutions, bonds, debentures and annuities. Currently there are relatively higher levels of taxation applying to interest income, compared to other forms of investment income. The discount will be available for interest income earned directly as well as indirectly, such as via a trust or managed investment scheme, and is expected to benefit around 5.7 million taxpayers in 2011-12.

There will be a flow-on effect for taxpayers claiming the discount for interest income as they will have a reduced adjusted taxable income. The Government will consult during 2010-11 on details concerning the operation of the discount, including in relation to the scope of the discount and the mechanism for applying the discount to interest earned indirectly by individuals.

Comment

To generate $1,000 of interest a taxpayer would need savings of $16,667 assuming a 6% interest rate.

As there is no preservation or holding period requirement apparently included in this measure, the 50% savings discount provides an alternative shorter-term savings mechanism, particularly for those affected by super contributions caps. However, over the longer term the taxation concessions applying to super do provide greater scope for increased savings, as shown in the following comparison.

	Inside super	**Outside super – no discount**	**Outside super – 50% discount on interest**
Initial investment	$20,000	$20,000	$20,000
Return in year 1	$1,200	$1,200	$1,200
Tax on returns in year 1	$180	$378	$221
Financial position after year 1	$21,020	$20,822	$20,980
Financial position after year 10 (inflation adj.)	$24,473	$22,263	$23,677

Assumptions: Investment returns (all income) of 6% pa, net of fees but before tax of 15% in super, 31.5% marginal income tax rate outside super, adjusted for the 50% savings discount as noted, inflation of 3% pa.

Note that this measure applies only to individuals (directly or indirectly through trusts or managed funds) but not to super funds or insurance companies (ie insurance bonds). However, the reduction in the company tax rate announced as part of the Government's response to the Henry Tax Review would otherwise increase net returns in the latter case.

Personal tax rate reductions already legislated from 1 July 2010

In accordance with the tax cuts announced in the 2008 budget, the personal income tax thresholds for the 2010- 2011 year will be as follows:

Income threshold	**Tax rate**
$0 - $6,000	0%
$6,001 - **$37,000**	15%
$37,001 - $80,000	30%
$80,001 - $180,000	**37%**
$180,000+	45%

These personal tax rates differ from the tax rates for 2009-2010 in that the income threshold for the 30% tax rate has been increased from $35,000 to $37,000 and the 38% tax rate has been reduced to 37%.

Additionally, the low income tax offset will increase to $1,500 from its current $1,350 with the upper income threshold being raised to $67,500 from $63,750.

Comment

If you have implemented a transition to retirement strategy you may wish to amend the amount you are salary sacrificing to take into account the new $37,000 threshold and the 37% tax rate.

Standard tax deduction from 1 July 2012

The Government plans to introduce a standard deduction for work-related expenses and the cost of managing tax affairs. The standard deduction will be $500 for the 2012/13 financial year, and then $1,000 for the 2013/14 and subsequent financial years.

Where a person's deductible expenses exceed the standard deduction amount, they will be able to claim the higher expenses instead of the standard deduction.

Comment

This standard deduction would be available regardless of whether relevant expenditure was actually incurred. For example, a person who completes their own tax return would be able to claim a deduction for their own efforts. The standard deduction will translate into a $157.50 saving for a person on a 30% marginal tax rate in the first year of the measure, and a $315 saving in subsequent years.

The combined effect of the 50% savings discount and the standard tax deduction is summarised in the following table:

	2010-11	**2011-12**	**2012-13**	**2013-14**		
Taxable income ($)	**Tax cuts ($)**	**Interest discount ($)**	**$500 standard deduction**	**Extra $500 of standard deduction**	**Total tax benefit compared to 2009-10 ($)**	**Tax benefit as a % of tax paid (including ML) in 2009 -10**
15,000	-	-	-	-	-	
20,000	150	83	17	83	332	37%
25,000	150	83	17	83	332	18%
30,000	150	83	17	83	332	12%
35,000	150	103	21	103	376	10%
40,000	450	178	36	178	841	15%
45,000	450	178	36	178	841	12%
50,000	450	178	36	178	841	9%
55,000	450	178	36	178	841	8%
60,000	450	178	36	178	841	7%
65,000	400	178	36	178	791	6%
70,000	300	158	32	158	647	4%
75,000	300	158	32	158	647	4%
80,000	300	158	32	158	647	3%
85,000	350	193	39	193	774	4%
90,000	400	193	39	193	824	4%
95,000	450	193	39	193	874	3%
100,000	500	193	39	193	924	3%
110,000	600	193	39	193	1,024	3%
120,000	700	193	39	193	1,124	3%
130,000	800	193	39	193	1,224	3%
140,000	900	193	39	193	1,324	3%
150,000	1,000	193	39	193	1,424	3%
160,000	1,100	193	39	193	1,524	3%
170,000	1,200	193	39	193	1,624	3%
180,000	1,300	193	39	193	1,724	3%
190,000	1,300	233	47	233	1,812	3%
200,000	1,300	233	47	233	1,812	3%
250,000	1,300	233	47	233	1,812	2%

Assumptions: the individual receives at least $1,000 pa of interest income and has existing deductions for work related expenses and cost of managing tax affairs of $400 per annum, which are replaced with a standard deduction. Net tax in 2009-10 refers to the net income tax plus Medicare levy liability of an individual, assuming application of the 2009-10 Medicare levy thresholds for a single person, entitlement to Low Income Tax Offset and no entitlement to any other tax offsets. Source: 2010 Budget papers

Increased Medicare levy low income threshold from 1 July 2009

The Government will increase the Medicare levy low income threshold to $18,488 for individuals and $31,196 for families. The additional amount of threshold for each dependent child or student will also increase to $2,865.

The Medicare levy threshold for pensioners below age pension age will also be increased to $27,697. This is to ensure that pensioners below age pension age will not have a Medicare liability where they don't have an income tax liability.

Technical amendment to SATO from 1 July 2010

The Government proposes to amend the senior Australians tax offset (SATO) regulations affecting the calculation of the rebate threshold, which is the amount of rebate income that can be earned before SATO is reduced. Currently, the formula, which is based in part on the low income tax offset (LITO), fails to reflect the fact that LITO reduces when taxable income exceeds $30,000.

Comment

This is a technical amendment which requires further clarification as to its operation and implications.

Capital protected borrowings – increase to benchmark interest rate from 11 May 2010

The Government has proposed to increase the benchmark interest rate that applies to capital protected borrowings to the Reserve Bank of Australia (RBA) indicator rate for standard variable housing loans plus 100 basis points. Prior to this announcement the benchmark interest rate was set at the RBA indicator rate for standard variable housing loans.

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

Comment

Increasing the benchmark interest rate by 100 basis points will allow existing borrowers to claim a larger proportion of the expenses on the borrowings as a deduction. This announcement could also make these products more attractive to some investors.

Net medical expenses tax offset from 1 July 2010

The Government plans to increase the threshold above which a taxpayer may claim the net medical expense tax offset (NMETO) from $1,500 to $2,000. This threshold will be indexed to the Consumer Price Index (CPI) on an annual basis.

Comment

This measure reduces the overall amount of tax offset a taxpayer could claim under the NMETO. Currently, taxpayers can claim a tax offset equal to 20% of net unreimbursed eligible medical expense above $1,500 for themselves or eligible dependants. Eligible medical expense includes ongoing aged care fees and charges, dental and optical expense, laser eye surgery etc.

Managed Investment Trusts – Government's response to the Board of Taxation's review – effective from 1 July 2011

The Government plans to introduce a new taxation regime for Australian managed Investment trusts (MITs) in response to the Board of Taxation's Report on its review of the tax arrangements applying to MITs. The new regime, amongst a range of changes, will allow MITs to use an attribution method of taxation (in lieu of the existing present entitlement to income method), as well as allowing unit holders, in some circumstances, to make adjustments to the cost base of their unit holding to eliminate double taxation.

Comment

The new regime should provide more certainty and simplification on taxation of MITs to both the trustees and beneficiaries.

Superannuation

Co-contribution – permanent reduction to matching rate and maximum payable

The matching rate of 100 per cent and the maximum co-contribution that is payable on an individual's eligible personal non-concessional contribution of $1,000 is proposed to be permanently retained.

Comment

Under announcements made in the 2009 Budget the co-contribution matching rate was to be reduced from 150% to 100% before being increased to 125% and then back to 150% as follows:

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Matching rate	100%	100%	100%	125%	125%	150%
Maximum co-contribution	$1000	$1000	$1000	$1250	$1250	$1500
Reduction rate for each $ above threshold	3.333 cents	3.333 cents	3.333 cents	4.167 cents	4.167 cents	5 cents

Under the 2010 Budget announcement this planned increase will not proceed and the maximum rate of co-contribution will be capped at $1000, as shown in the shaded section.

Co-contribution - indexation of income thresholds paused for two years from 1 July 2010

The Government plans to freeze for 2010/11 and 2011/12 the indexation applied on the income threshold above which the maximum superannuation co-contribution begins to phase down.

The maximum co-contribution of $1,000 is reduced by 3.333 cents for every dollar that a taxpayer's total income exceeds $31,920 until it reaches or exceeds $61,920.

Comment

Effectively this measure will freeze these thresholds at $31,920 and $61,920 for the next two financial years (ie 2010/11 and 2011/12).

ATO discretion on excess contributions tax assessments

This measure proposes giving the Commissioner the ability to exercise its discretion prior to an assessment being issued for excess contributions tax.

Comment

Currently, a taxpayer may apply to the Commissioner for a determination that part or all of their excess contributions be disregarded or reallocated to another income year. Such an application must be made within 60 days of receiving an excess contributions tax assessment, which also includes the taxpayer's excess contributions tax liability. This measure would allow an application to be made prior to receiving the assessment, potentially allowing a person to have a decision made before having to pay excess contributions tax.

Super fund deductions for terminal medical conditions benefits from 16 February 2008

The Government has announced that it will be seeking to extend the number of benefits that are deductible for complying super fund and retirement savings account providers to include terminal medical conditions (TMC).

Comment

The measure seeks to address the current anomaly in taxation laws where deductions are only allowed for benefits relating to death, permanent incapacity and temporary incapacity conditions of release. This will allow super fund providers to be able to recoup the costs of paying out TMC claims and ensure these can be paid out in a more timely fashion.

Eligible super contribution deductions extended permanently for successor superannuation funds effective from 1 July 2010

The Government has announced plans to permanently allow a claim for a deduction for eligible contributions to be made to successor superannuation funds.

Comment

This measure would allow a deduction notice to be lodged with a success fund where the relevant contributions were actually made to the transferring fund. Accordingly, it addresses a current inequity in superannuation laws which deny investors a perfectly legitimate tax deduction due to circumstances mainly out of their hands. Usually investors do not have any control over the transfer of their current benefits from one super fund to another if it is based on a successor fund transfer.

Other amendments to super contributions from 2010-11

The Government will introduce a number of measures to improve the eligibility for a tax deduction on superannuation contributions.

These are:

- To increase the time-limit for deductible employer contributions for former employees (currently two months after termination).
- To clarify the due date of the shortfall interest charge for the purposes of excess contributions tax.

Comment

These measures will make some of the timeframes more reasonable and in line with when individuals and employers would engage in these activities.

Changes to First Home Owners Savers Accounts (FHSA) scheme from date of assent

The Government proposes that savings in an FHSA can be paid into an approved mortgage after the end of a minimum qualifying period, rather than requiring it to be paid to a superannuation account.

The current rules require that FHSA holders keep their savings in an FHSA for 4 financial years before they are able to use those savings to buy a home. At present if an account holder buys a home before the end of that 4-year period, the balance of their FHSA must be transferred to their superannuation.

The changes will apply for houses purchased after assent of the legislation that will give effect to this measure.

Comment

This measure will allow an earlier access to the savings instead of waiting to meet a condition of release under superannuation rules and the ability to reduce mortgage debt.

Social Security and Family Assistance

Family Tax Benefit non-lodgement suspensions - exemptions

In the 2008 Budget, the Government had proposed to suspend FTB payments to people who had not lodged their tax return in 12 months and had not responded to Centrelink requests to do so. This measure will be retained with two exceptions. Payments will continue to people who do not have any FTB debt, or where ceasing the payments would cause undue hardship.

Family Tax Benefit –A: Strengthening participation requirements from 1 July 2010

In the 2009 Budget, the Government extended FTB Part A to cover children aged 16-20 who do not have a Year 12 or equivalent qualification, and who participate in full-time education or training, or part-time education or training in combination with other approved activities.

The participation measure will now be strengthened. Children will now be required to participate in full-time education or training. Part-time education or training will not be sufficient. These participation requirements will be introduced when the measure commences on 1 July 2010.

Child Care Rebate capped from 1 July 2010

The Child Care Rebate will be capped at $7,500 per child (2008/09 level) from the current annual cap of $7,778 per child. Also indexation of the cap will be paused for four years from 1 July 2010. The out-of-pocket reimbursement of child care expenses will remain at 50 per cent up to the annual cap.

Expanded Special Disability Trust criteria from 1 January 2011

The Government will amend the eligibility criteria and allowable uses for Special Disability Trusts. The definition of a beneficiary will be expanded to include people with a disability who can work up to seven hours per week.

The allowable uses for the trust will be expanded to include all medical expenses, including membership costs of private health funds, maintenance expenses of Special Disability Trust property and discretionary spending of up to $10,000 per year

Comment

This measure will further encourage the uptake of Special Disability Trusts by increasing trust expenditure criteria and make the trusts more accessible to those who were previously excluded because of their limited employment.

Disability Support Pension (DSP): refined assessment process

When determining eligibility for the DSP Centrelink will have a greater focus on the individual's potential to work. Claimants who do not have sufficient evidence to demonstrate that they cannot be assisted back to work will have their DSP claim rejected and will instead be referred to an employment service to build their employment capacity. Claimants who are clearly unable to work will not be affected, including those with profound disability, serious medical conditions or terminal illness.

In addition to these changes from 1 July 2010, assessment for the DSP will be simplified to fast-track more claimants who are clearly eligible due to a cancer, congenital or catastrophic disability.

Comment

Clients who are looking to claim the DSP may be affected by these measures depending on their individual circumstances; those with manifest disability will benefit from a quicker assessment whereas others may be rejected.

Henry response confirmation

As expected, the 2010 Budget reiterated the Government's commitment to the following proposals announced in response to the Henry Tax Review:

- Increase of super guarantee rate from 9% to 12%, commencing 1 July 2013.
- Raising the super guarantee maximum eligibility age to 75 from 70.
- Introducing a 15% low income earners Government contribution capped at $500, effectively refunding contributions tax on up to $3,330 of concessional contributions.
- Retaining the $50,000 concessional cap for those age 50 or over who have super balances of less than $500,000.
- Reducing the standard company tax rate to 29% from 1 July 2013 then 28% from 1 July 2014.
- Reducing the small business company tax rate to 28% from 1 July 2012.
- Allowing small businesses to immediately write off assets valued at under $5,000 and other assets in a single 30% rate depreciation pool.