

## Contents

Introduction .....	1
Government proposals .....	2
Henry Review recommendations ruled out.....	6
Henry Review other key recommendations .....	7
Pre-announcement speculation .....	18
Where to now?.....	19

## Introduction

The Government has released its response to the Henry review into taxation. Largely funded by a new Resource Super Profits Tax, the reforms include some key changes to superannuation and company taxation.

Major changes to superannuation include a phased increase in the rate of superannuation guarantee from 9 per cent to 12 per cent, the extension of the superannuation guarantee for workers aged between 70 and 75, a Government contribution of \$500 for low income earners and the doubling of allowable concessional contributions from 1 July 2012 for workers aged 50 and over with less than \$500,000 in superannuation.

Key changes to taxation include the gradual reduction in the company tax rate to 28% and simplified rules for small business depreciation.

This FirstTech Henry Tax Review Briefing provides a summary of these and other relevant announcements and how they may affect your clients.

# Government proposals

## Superannuation

### Increasing super guarantee rate to 12%

The SG rate will be increased gradually with initial increments of 0.25 percentage points on 1 July 2013 and 1 July 2014. Further increments of 0.5 percentage points will apply annually up to 2019-20, when the rate will be set at 12%.

**Table 1 - Proposed SG timeline**

Year	SG Rate (%)
2009-10	9
2010-11	9
2011-12	9
2012-13	9
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

### Implications

Increasing the SG rate in the manner proposed will provide for higher super balances, particularly for younger individuals. For example, a 30 year old with a \$30,000 current super balance earning a salary of \$60,000 per year could see their super balance increase by \$194,000 in nominal terms, or \$69,000 in real terms. This assumes investment returns of 7.7% pa net of fees and inflation of 3% pa.

### **Raising super guarantee age limit to 75**

From 1 July 2013, the age limit for payment of super guarantee contributions will be increased from 70 to 75. This will bring the SG age limit into line with that for personal and voluntary employer contributions.

### Implications

The Government estimates 33,000 employees will benefit from this measure. The combination of an increased SG rate and longer availability mean that a person who will continue working until age 75 may see an increase in their retirement savings of \$232,050 in today's dollars. This assumes investment returns of 7.7% pa net of fees and inflation of 3% pa.

### **Low income earners government contribution**

The Government will provide a contribution equal to 15% of concessional contributions made, up to \$3,333, for low income earners with an adjusted taxable income of up to \$37,000. The maximum Government contribution paid will be \$500 (not indexed).

This measure will apply to contributions made from 1 July 2012, with the first Government contributions expected in 2013-14.

This measure will apply to concessional contributions, including super guarantee contributions. It means that a person with an adjusted taxable income (ATI) of up to \$37,000 will effectively not pay contributions tax on their SG contributions. The measure makes super contributions tax neutral for those on a 0% and a 15% marginal tax rate, as shown in Table 2. Note that from 1 July 2010, the 15% MTR will apply on incomes up to \$37,000.

**Table 2 – Effect of low income earners Government contribution for employees**

	<b>Current position</b>	<b>Proposal</b>
Salary	\$37,000	\$37,000
9% SG contribution	\$3,330	\$3,330
Contribution tax	\$500	\$500
Government contribution	NIL	\$500
Net contribution	\$2,830	\$3,330

Low-income earning self-employed people will similarly benefit from the effective removal of contributions tax on deductible contributions. As shown in Table 3, clients in this situation will be able to maximise their net super contributions through a combination of personal deductible and co-contributions.

**Table 3 – Effect of low income earners Government contribution for self-employed clients**

<b>Income level</b>	<b>Personal deductible contribution only</b>	<b>NCC + co-contribution</b>	<b>Personal deductible + NCC + co-contribution</b>
\$30,000	\$3,330	\$3,281	\$3,870
\$31,000	\$3,330	\$3,281	\$3,870
\$32,000	\$3,330	\$3,278	\$3,869
\$33,000	\$3,330	\$3,245	\$3,851
\$34,000	\$3,330	\$3,212	\$3,833
\$35,000	\$3,330	\$3,178	\$3,815
\$36,000	\$3,330	\$3,145	\$3,797
\$37,000	\$3,330	\$3,112	\$3,779

Assumptions: marginal tax rate of 31.5%, low income earners Government co-contribution applies to reduce effect of contributions tax to 0%, maximum pre-tax contribution \$3,330, combination of personal deduction + NCC + co-contribution assumes maximum co-contribution for level of income, with remainder of pre-tax amount used for a personal deductible contribution.

### Implications

Should this measure be implemented using similar mechanics as the existing Government co-contribution, eligible low income earners will need to ensure they lodge a tax return.

### **Higher concessional contributions caps retained for over-50's**

From 1 July 2012 the higher \$50,000 concessional contribution cap will be extended permanently for individuals aged 50 or over who have total superannuation balances of less than \$500,000.

This measure will enable those with lower superannuation savings to make additional 'catch-up' contributions close to retirement, for example:

- individuals who have not had the benefit of a full working life of superannuation
- those who take time out of the workforce as care-givers to young children, the elderly and those with a disability.

The Government will consult with the super industry on the operation of the \$500,000 threshold. Note that superannuation funds currently report end of financial year account balances to the ATO through the member contribution statement.

### Implications

Presumably 'superannuation balances' will include both accumulation and pension balances, so those implementing transition to retirement strategies at preservation age will need to take account of both balances in determining necessary salary sacrifice contributions. However, an increased concessional cap past 1 July 2012 should ensure continued use of this valuable strategy.

### **Company Taxation**

The Government will reduce the company tax rate from its current level of 30% to 29% for the 2013-14 income year and to 28% from the 2014-15 income year. Eligible small businesses will receive the tax cut one year earlier with a company tax rate of 28% from the 2012-13 income year.

This reduction will have little real impact on Australian resident shareholders due to the imputation system. However, this is a direct tax reduction for non-resident shareholders who are not eligible for imputation credits.

### **Small business taxation**

#### **Expanding capital allowances concessions for small businesses**

This measure will commence from 1 July 2012 and will enhance and expand the existing capital allowance concessions available for small businesses by:

- Allowing small businesses to immediately write-off assets valued at under \$5,000 (up from \$1,000); and
- Allowing small businesses to write-off other assets, with the exception of buildings, in a single depreciation pool at a rate of 30%.

### **Resource Super Profits Tax**

A key part of the Government's response to the Henry review is the proposed Resource Super Profits Tax (RSPT). While likely to have limited direct impact on financial planning activities and investment products, it is important to note that the Government's progress on other elements of its tax reform agenda will be dependent on the revenue derived from the RSPT.

A Resource Super Profits Tax (RSPT) will be introduced on 1 July 2012 at a rate of 40% on profits made from exploitation of non-renewable resources. It will replace the crude oil excise and operate in parallel with State and Territory royalty regimes, with the latter providing a refundable credit to the resource entity. The Government will consult extensively on the design of the RSPT.

## Henry Review recommendations ruled out

In the interests of business and community certainty, the Government advises that it will not implement the following policies at any stage. Some of these are recommendations of the Australia's Future Tax System review; some are potential misinterpretations of the recommendations:

- include the family home in means tests (see Rec 88c)
- introduce land tax on the family home – this is a state tax and thus an issue for the states (see Rec 52 & 53)
- require parents to work when their youngest child turns 4 (see Rec 85)
- hit single income families (see Rec 92 & 93)
- restrict eligibility to rent assistance for families (see Rec 103)
- do any changes to the tax system that harm the not-for-profit sector, including removing the benefit of tax concessions, raising the gift deductibility threshold or changing income tax arrangements for clubs (see Rec 9e, 13, 41, 43 & 44)
- reduce overall remuneration to the members of our defence forces (see Rec 6d, 8c & 9e)
- reduce the CGT discount, apply a discount to negative gearing deductions, or change grandfathering arrangements for CGT (see Rec 14 & 17c)
- remove the Medicare levy (see part of Rec 5)
- reduce indexation of the age pension (see Rec 84)
- remove the benefits of dividend imputation (see Rec 37)
- think of hitting pensioner and low income concessions for utilities, transport and other essential services (see Rec 107)
- introduce a bequests tax (see Rec 25)
- align preservation age with pension age (see Recommendation in AFTS Retirement income strategic issues paper)
- offer a government annuity product (see Rec 22)
- ask the States to charge market rents to public housing recipients (see Rec 106)
- abolish the Luxury car tax (see Rec 80)
- index fuel tax to CPI (see Rec 65)
- change alcohol tax in the middle of a wine glut and where there is an industry restructure underway (see Rec 71) .

The Government has also reaffirmed that it will never increase the rate or broaden the base of the GST or remove tax free superannuation payments for the over-60s, which were both ruled out of the Henry Review Terms of Reference.

## Henry Review other key recommendations

### Tax and transfer system for 21<sup>st</sup> century

#### **A robust and efficient broad based system**

Revenue raising should be based on four robust and efficient broad-based taxes

- personal income, assessed on a more comprehensive basis
- business income, designed to support economic growth
- rents on natural resources and land
- private consumption.

Additional specific taxes should exist only where they improve social outcomes or market efficiency. Revenue should only be a by-product of any specific tax or charge and should not be the reason for it. Other existing taxes should be abolished.

(Recommendation 1)

#### **Personal taxation**

##### **Simplify the personal income tax rate scales**

The personal income tax rate scales should be simplified so that a high tax-free threshold applies with income above that level taxed at a constant marginal rate for most people.

Although the final report makes no recommendations in relation to where the tax free threshold should be set or the rate of tax that should apply, it does provide an example of such a system that involves the following:

- a tax free threshold set at \$25,000
- a flat tax rate of 35% applying to incomes from \$25,000 to \$180,000
- a 45% tax rate applying to incomes above \$180,000.

(Recommendation 2)

##### **Individuals to continue as the primary tax unit**

The primary unit in the tax system should continue to be individuals (not couples) and concessions for dependants should be restricted (see Recommendation 6).

(Recommendation 3)

##### **Income support and supplementary payments should be tax exempt**

(Recommendation 4)

##### **Reform structure of tax offsets**

The Medicare Levy and structural tax offsets (i.e. the low income, senior Australians, pensioner and beneficiary tax offsets) should be removed as separate components and incorporated into the personal income tax rates scale.

*Note – the Government has advised it will not be adopting this recommendation.*

(Recommendation 5)

##### **Remove, rationalise or replace concessional offsets**

To remove complexity and ensure government assistance is properly targeted:

- a. existing dependency offsets should be replaced with a single tax offset
- b. the zone tax offset should be reviewed
- c. the mature age worker offset, employment termination payment, overseas civilian, entrepreneurs' and notional tax offsets should be removed. The

education tax refund should be replaced with a back to school lump sum amount

d. the overseas forces tax offset should be replaced by adjusting remuneration

e. averaging tax offsets for farmers, the offset for special professionals and the lump sum payment in areas offset should be retained.

(Recommendation 6)

### **Review health-related tax concessions**

Remove or review concessions consistent with the National Health and Hospitals Reform Commission recommendations:

- the medical expenses tax offset should be removed following a review
- the Medicare levy surcharge and assistance for private health insurance should be reviewed.

(Recommendation 7)

### **Equivalent taxation of all forms of wages and salary**

All forms of wages and salary should be taxed on an equivalent basis without exemption.

a. Private education payments in respect of employment and employment related payments should be assessed as income.

b. The broad exemptions for foreign employment income should be removed.

c. Defence force payments should be taxable and remuneration increased.

*Note – the Government has advised it will not be adopting this recommendation*

(Recommendation 8)

### **Administration of fringe benefits**

The scope of fringe benefits that are subject to tax should be simplified, with a number of recommendations made relating to how this may be achieved, including:

- Using market value to value fringe benefits.
- Fringe benefits that are readily valued and attributable to individual employees should be taxed in the hands of employees through the PAYG system.
- Car fringe benefits should be valued with a single statutory rate of 20 per cent, regardless of the kilometres travelled.
- Not-for-profit entities' FBT concessions should be reconfigured.
- Other fringe benefits should remain taxed to employers at the top marginal rate and non-reportable for employees.

*Note – the Government has advised it will not make any changes that harm the non-for profit sector or reduce overall remuneration to defence force members.*

(Recommendation 9)

### **Alienation of personal services income**

Revised regime to prevent the alienation of personal services income, where a significant proportion of the business income is generated from the personal services of the owner-managers, whether in employee-like or non-employee-like cases.

This regime may also apply an arm's length rule to deductions arising from payments to associates, to ensure deductions reflect the value of services provided.

(Recommendation 10)

### **Standard tax deduction**

An automatic standard deduction should be introduced, to simplify and facilitate more pre-filling of tax returns, unless a person's actual expenses exceed the standard deduction amount. Where the person's actual expenses exceed the standard deduction amount, they are able to choose either to take the standard deduction or to claim actual expenses, with full substantiation.

(Recommendation 11)

### **Deductibility of expenses**

There should be a tighter nexus between the deductibility of the expense and its role in producing income.

(Recommendation 12)

### **Gift deductibility**

Gift deductibility should be retained, with the deductibility threshold raised from \$2 to \$25.

*Note – the Government has advised it will not make any changes that harm the not-for profit sector.*

(Recommendation 13)

## **Taxation of income from savings**

### **40% discount on savings**

- Provide individuals with a 40% discount on savings income for non-business related:
  - net interest income
  - net residential rental income (including related interest expenses) - following reforms to the supply of housing, and reforms to housing assistance (as per recommendations on housing affordability & housing assistance).
  - capital gains (and losses)
  - interest expenses related to listed shares held by individuals as non-business investments
- Interest expenses in relation to investments in listed companies should be discounted given the difficulties in assigning debt to particular investments and the significant tax benefits that would otherwise still remain for margin lending.
- Further consideration should also be given to addressing the taxation treatment of individuals owning shares, regarding when the shares are held on capital account (and subject to capital gains tax) and on revenue account (and taxed as ordinary income), as this will affect eligibility for the 40% discount.
- A smooth transition to the 40% savings discount should be provided to minimise any disruption.
- As part of the consideration of alternative company income tax arrangements and dividend imputation (see recommendations 26 and 37), consideration should be given to the possibility of extending the discount to other savings income.

*Note – the Government has advised it will not apply a discount to negative gearing deductions.*

(Recommendations 14, 15 and 16)

## **Simplify the capital gains tax (CGT) regime**

The CGT regime should be simplified by:

- exempting all personal use assets and increase exemption threshold for collectables
- rationalising small business CGT exemptions by:
  - removing the 50% active asset and 15 year exemptions
  - aligning the \$500,000 retirement exemption with the CGT cap for contributions (currently \$1.1M)
  - allowing taxpayers who sell a share in a company or an interest in a trust to access concessions via the turnover test
- removing the concessions for pre-CGT assets. Also the cost base of pre-CGT assets should be set at market value on the date the concession is removed or before the end of previous indexation arrangements
- rewrite the CGT legislation to better integrate it with rest of the income tax system .

*Note – The Government has advised it will not be reducing the CGT discount or change CGT grandfathering arrangements.*

(Recommendation 17)

## **Retirement incomes**

### **Abolish taxation of super contributions**

- Retirement incomes should be improved by removing contributions tax.
- Employer superannuation contributions should be treated as employee income, with employees receiving a flat-rate tax offset.
- Access to concessions should be broadened by making voluntary contributions up to \$25,000 pa (\$50,000 for people age 50 or more) eligible for the offset.

(Recommendation 18)

### **Reduction of super fund earnings tax**

- The rate of tax on superannuation fund earnings should be reduced to 7.5%.
- The 7.5% tax should also apply to capital gains without a discount and the earnings from assets supporting superannuation income streams.
- Superannuation funds should retain their access to imputation credits.

(Recommendation 19)

### **Allow contributions past age 75**

- Work test should remain for people aged 65 and over, but lift the restriction on people aged 75 and over from making contributions.
- No restrictions on people wanting to purchase longevity insurance products from a prudentially regulated entity.

(Recommendation 20)

### **Development of longevity products**

- The government should support the development of longevity products and better facilitate their provision by the private sector ie. the issue of long-dated bonds .

(Recommendation 21)

## **Retirement income streams**

The government should consider offering an immediate annuity and deferred annuity product and remove rules that restrict the development of income stream products.

Compulsory purchase of such products is not recommended.

*Note – the Government has advised it will not be adopting this recommendation.*

(Recommendation 22)

## **Payment of super guarantee contributions**

Require superannuation guarantee contributions to be paid at the same time as wages, linking superannuation records. Develop a single portal through which people could interact with government agencies.

(Recommendation 23)

## **Preservation age for service pensioners unchanged**

- The super preservation age should remain at 60 for Service Pensioners (note the recommendation in May 2009 to align preservation and pension eligibility ages)

(Recommendation 24)

## **Company taxation**

### **Retain current company tax system**

The structure of the company income tax system should be retained in its present form, at least in the short to medium term. Consideration should be given to the introduction of a business level expenditure tax.

(Recommendation 26)

### **Reduce company tax rate to 25%**

The company income tax rate should be reduced to 25 per cent over the short to medium term. Note that the Government has partially implemented this measure, reducing the company tax rate to 29% from 1 July 2013 and 28% from 1 July 2014.

(Recommendation 27)

### **Dividend imputation**

Dividend imputation should be retained, but for the longer term, consideration should be given to alternatives as part of a further consideration of company income tax arrangements.

A flow-through entity regime for closely held companies and fixed trusts would merit further consideration if there is a move away from dividend imputation. While dividend imputation is retained, imputation credits should continue to be provided only for Australian company income tax. Dividend streaming and franking credit trading practices should, in general, continue to be prohibited.

*Note – the Government has advised it will not remove the benefits of dividend imputation*

(Recommendations 37, 38 and 39)

### **Streamline capital allowance arrangements**

Streamline and enhance the capital allowance arrangements for both large and small businesses. The recommended small business measures have been taken up in part by the Government, as follows -

- Instant write-off for depreciating assets worth up to \$5,000; and
- allowing all other depreciating assets (except buildings) to be pooled together, and depreciated at a rate of 30%.

(Recommendations 28 and 29)

### **Small business taxation**

#### **Amend small business entity definitions**

The small business entity turnover threshold should be increased from \$2 million to \$5 million, and adjustments to the \$6 million net asset value test should be considered.

Further recommendations have been made in relation to rationalising and streamlining the current small business CGT concessions.

(Recommendation 30)

### **Non-residents**

#### **Interest withholding tax**

Financial institutions operating in Australia should generally not be subject to interest withholding tax on interest paid to non-residents. Consideration should be given to negotiating, in future tax treaties, a reduction in interest withholding tax to zero (with safeguards to limit tax avoidance).

(Recommendations 33 and 34)

### **Managed funds and trusts**

#### **Improve managed funds taxation**

Taxation arrangements applying to Australian managed funds should be improved to provide greater certainty that conduit income will not be subject to Australian tax.

(Recommendation 35)

#### **Rewrite trust rules**

The current trust rules should be updated and rewritten to reduce complexity and uncertainty around their application.

(Recommendation 36)

### **Not-for-profit organisations**

#### **Continue income tax and GST concessions to not-for-profit (NFP) organisations**

NFP organisations that currently receive income tax or GST concessions should retain these concessions and should be permitted to apply their income tax concessions to their commercial activities.

(Recommendation 42)

### **Reconfigure not-for-profit (NFP) FBT concessions**

The capped FBT concessions for NFPs should be gradually reduced and phased out over ten years. Reportable fringe benefits for affected employees that are easily valued and attributed would be exempt from tax up to the relevant cap, and taxed at the employee's marginal tax rate above the cap.

- The market value of these benefits would be taken into account for transfer payment purposes.
- Non-reportable fringe benefits would be taxable for NFP employers.
- The FBT concessions should be replaced with direct government funding, to be administered by the relevant Australian government portfolio agencies or the charities commission.
- All NFP organisations eligible for tax concessions should be able to apply to the relevant body for funding for specific projects or for assistance with the costs of recruiting specialist staff.

*Note – the Government has advised it will not make any changes that harm the non-for profit sector.*

(Recommendation 43)

### **Uniform resource rent tax**

The introduction of a uniform resource rent tax imposed and administered by the Australian government at a rate of 40%. This will be adjusted to offset any future changes in the company tax rate from 25 percent to achieve a combined statutory tax rate of 55 per cent.

Note that the government intends to introduce this as the Resource Super Profits Tax (RSPT) tax from 1 July 2012 on the basis that it will provide a better return to the Australian community compared with the current arrangements. It believes this to be a more efficient mechanism to collect the appropriate financial return from resources to be re-directed back to the community.

Furthermore, the resource rent tax needs to be sustainable and should not provide concessions to encourage exploration or production activity at a faster rate than the commercial rate or in particular geographical areas, and should not allow deductions above acquisition costs to stimulate investment.

(Recommendations 45 and 46)

### **Land and property taxes**

As one of the solutions in addressing housing affordability the review has recommended the removal of stamp duty and instead the broadening of land taxes as a more efficient tax collecting method.

#### **Remove stamp duty**

Stamp duty should be removed and instead be covered by more efficient tax rates through broadening land tax. It is envisaged that this will have a downward pressure effect on house prices.

(Recommendation 51)

### **Broaden and improve operation of land tax**

Land tax should be broadened due to the efficiency in collecting this revenue. In order to tax more valuable land at higher rates, consideration should be given to levying land tax using an increasing marginal rate schedule.

Further, land tax should be broadened to include all land with measures in place to reduce the effect on low value lands.

To improve the operation of land tax, eliminate stamp duties on commercial and industrial properties in exchange for a broad land tax and investigate the necessary arrangements during the transition phases. *Note – the Government has advised it will not be adopting this recommendation.*

(Recommendations 52, 53 and 54)

### **Consumption Tax**

Over time, a broad-based cash flow tax could be used to finance the abolition of other taxes, including payroll tax and State insurance taxes. From a policy making perspective, it is important for the Government to raise revenue from an efficient and sustainable tax base. Consumption is generally less volatile than income or wealth, and therefore provides a more stable revenue source.

(Recommendation 55)

### **Abolish specific taxes on insurance**

Currently, all States impose duties at various rates on premiums charged for insurance products, such as general insurance, life insurance, term insurance and health insurance. The recommendation is to abolish any such specific taxes and levies.

(Recommendation 79)

### **Government Income Support Payments**

#### **Categorise income support payments**

Income support payments should be categorised into three categories:

- pension category – for people who are not expected to support themselves through paid work, as a result of their age, disability, or carer obligations. Rates should provide a basic acceptable standard of living.
- participation category – for people of working age who are expected to support themselves through paid work. This would cover those who are temporarily incapacitated, people with partial capacity to work and primary carers of dependent children. Rates should provide basic level of adequacy while maintaining incentives to work.
- A student assistance category for people engaged in full-time study. Rates would be lower than payments to the unemployed.

There should be a more consistent approach to payment relativities within each of the three income support categories based on the single and couple pension relativities. Payments and income test parameters should be indexed in a consistent way with the indexation reviewed on a regular basis.

*Note – the Government has advised it will not reduce indexation of the age pension*

(Recommendations 82, 83 and 84)

### **Arrangements for parents**

Income support arrangements for parents should support and encourage work while maintaining adequate levels of assistance for families. As a condition of payment parents should be required to look for part-time work once their youngest child turns four. Supplement payments should then vary depending on the age of the oldest and youngest child. *Note – the Government has advised it will not be adopting this recommendation.*  
(Recommendation 85)

### **Work requirement and certain income support payments**

People with disability who have a partial capacity to work (except people receiving Disability Support Pension) should have a part-time work requirement. Students should have access to an income test that facilitates significant part-time work at a level that does not compromise education outcomes. Adults requiring additional income should be able to borrow to top up their student rate of income support to the level of the participation payment rate.  
(Recommendations 86 and 87)

### **Change means test for income support payments**

The current means test for income support payments should be replaced with a comprehensive means test based on a combined measure of employment income, business income and deemed income on assets, with features including:

- extending deeming to a broader range of assets in addition to financial assets, including superannuation account based pensions, rental housing and holiday homes, personal-use assets above an exempted cap and other asset classes (whether income-producing or not).
- exempting owner-occupied houses from the means tests only up to a certain cap. *Note – the Government has advised it will not be adopting this recommendation.*
- retaining the work bonus for people over age pension age.
- retaining the current different income free areas for pensions and allowances.
- Remove the liquid assets waiting period and sudden-death asset test cut-out that applies to certain payments such as Newstart Allowance, Partner Allowance, Sickness Allowance.

(Recommendation 88)

## **Family and youth assistance**

### **Replace Family Tax Benefit Parts A and B with a single payment**

Family Tax Benefit Parts A and B should be replaced with a single payment covering the direct costs of children in a low-income family.

### **Family assistance should be based on a per child basis**

Family assistance should be based on per child basis and increase with the age of the children to recognise the higher costs of older children. The Baby Bonus should be abolished and replaced with a small supplementary payment. A shared-care rate should be considered to recognise the higher costs of separated families taking into account interactions with child support as well as other income support payments. Additional payments and higher thresholds for larger families should be reconsidered.

### **Supplements for families nurturing young children**

A supplement for parents with young children aged less than six years should be provided as a per-family payment and should be means tested on family income

### **Payments for single parents with children aged over six**

A parental supplement should be paid through the family payment system for single parents with children aged six or older.

### **Payments for couples with children**

A parental supplement at the same rate as for single parents should be paid through the income support system for couples with children aged six or older.

### **Additional assistance for families with children with special and higher needs**

Assistance for families should also recognise that there are specific circumstances, such as parents caring for disabled children and foster care children with higher needs, for which additional support beyond the early years is appropriate.

### **Family assistance means test**

The total amount of family assistance should be withdrawn with a single means test to avoid cumulative withdrawal rates. A single low taper rate of 15–20 per cent would be appropriate to minimise workforce disincentives.

### **Youth payments should be available to older children**

Youth payments should be available to older children such as dependent older children leaving school and looking for work or combining part-time work and part-time study. Children without access to financial support from their families should continue to have access to a youth payment.

### **Youth payments main form of income support**

Youth payments should be the main form of income support from the age of 18 until the age of independence. Family means tests should be designed so that families with dependent children in both the family payments and youth payments system are not disadvantaged. The age of independence should be aligned for full-time students and non full-time students.  
(Recommendations 90 to 98)

## **Child care assistance**

### **Reforms to child care assistance**

Child Care Benefit and Child Care Rebate should be combined into a single payment:

- based on a percentage of costs
- means tested down to the base rate based on family income and
- should take into account income support, family payments and marginal tax rates, to ensure that effective tax rates are not excessive.

The fringe benefits tax exemption for child care facilities provided on an employer's business premises for the benefit of employees should be removed.  
(Recommendations 99, 100 and 101)

## Housing and rent assistance

### Reform of rent assistance

The maximum rate of rent assistance should be increased to assist renters to afford an adequate standard of dwelling and indexed by movements in national rents.

Rent assistance should be:

- part of the income support system with eligibility based on rent paid and the income support means test, rather than on eligibility for another payment. *Note – the Government has advised it will not be adopting this recommendation*
- extended to public housing tenants along with removing income-linked rent setting in public housing.

(Recommendations 102 to 104)

### Social housing

A high need housing payment should be paid to social housing providers for their tenants who have high or special housing needs or who may face discrimination in the private market.

Income linked rents should be phased out in social housing, with providers charging their tenants rents linked to the market rate, with existing rent-setting for current tenants phased out using grandfathering or other transitional arrangements.

(Recommendations 105 and 106)

## Pre-announcement speculation

### **Compulsory annuitisation**

There had been some speculation that a portion of retirement savings would need to be used to purchase a lifetime income stream. Although this has been addressed to some extent by recommending the Government support the development of a longevity insurance market (recommendation 21), there is no mention as to how much of a person's superannuation would need to be allocated to such a product.

### **Superannuation concessions reduced for high income earners**

On the surface there are no recommendations that reduce the concessional tax treatment for higher income earners. Instead the actual super contribution will be included in one's taxable income and taxed at the highest marginal tax rate as noted in recommendation 18. To ensure that lower income earners are not at a disadvantage a rebate will be provided to ensure that tax on their super contributions will not exceed 15%. In effect this will reduce the tax effectiveness of super contributions for higher income earners as the tax savings they will receive will not be as great under the proposed system. In addition it has also been recommended the government co-contribution and spouse contribution rebate be removed as a result of the introduction of the rebate on super contributions.

### **Increase to super contributions tax rate**

There had been some speculation that, in better targeting super tax concessions to lower income earners, the Government would increase the contributions tax rate and provide a tax offset for lower income earners. Instead, the Henry report recommends lowering the super fund earning tax rate and the Government has proposed an alternative mechanism for supporting lower income earners by providing a low income earners Government contribution.

### **Transition to retirement**

There are no specific recommendations or Government proposals addressing transition to retirement. However, the extension of the higher \$50,000 concessional contributions cap for those aged 50 or over will ensure continued use of this strategy.

### **CGT discount and tax benefits of negative gearing**

Despite the review recommending changes on investment losses and CGT (recommendations 14 & 17C), the government has decided at this stage not to make any changes to the existing systems.

### **Dividend imputation**

Imputation credits were an area earmarked for substantial change, however the review recommends that the government not make any changes in the short and medium term.

### **Align preservation age with pension age**

This was expected to be addressed further in the final report; however the Government has now clearly ruled this out. Hence the current preservation age rules will remain into the foreseeable future.

## Where to now?

The Government has commented that tax reform is a long term process and that its plan is a significant first step in that process, representing a full reform agenda for several years. The proposed resource super profits tax is an important part of that process, as progress on the initial elements announced on 2 May 2010 will depend on securing revenue from its implementation.

The Government has said that it will continue to develop its tax reform agenda over the coming years. In particular:

- The Government will consider how it can make the personal tax system simpler and more transparent
- The Board of Taxation has completed its review of the taxation arrangements applying to managed investment trusts and provided its report to the Assistant Treasurer.
- The Australian Financial Centre Forum has provided its report on *Australia as a Financial Centre* (the Johnson Report), with several Henry report recommendations in line with its recommendations.

The 2010 Federal Budget, to be handed down on Tuesday 11 May 2010, is likely to reiterate the Government's commitment to these proposals and provide details around funding and revenue implications.

## Disclaimer

The information contained in this Henry Review Briefing is based on the understanding Meridian Financial Group ABN 93 830 089 954 Authorised Representative of AMP Financial Planning Pty Ltd ABN 89 051 208 327 AFS Licence 232706, has of the published review materials and relevant Australian laws as at 3 May 2010 and is of a general nature only.

This briefing is not financial advice and does not take into account individual's objectives, financial situation or needs.