Tax Talk – April/May 2010

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Federal Budget Bulletin

Australia on the Potholed Road to Recovery

With falling revenues and a need to maintain spending in the wake of the Global Financial Crisis, Wayne Swan treads the tight rope to hand down his second Federal Budget. The Budget follows the trend of the Government's economic stimulus that is seen to be necessary to combat the Global Financial Crisis by identifying a multitude of infrastructure projects for roads, railways, ports, hospitals and schools. It appears some states have fared better than others in this lottery.

The Government has also maintained its election promises to increase the aged pension (with an extra $32per week for a single age pensioner) and to deliver the income tax cuts announced in the previous budget. At a time of falling tax receipts these important spending measures have to be paid for somehow and the Government has opted for a combination of increased debt and an attack on higher income earners' tax and welfare breaks. This Budget Bulletin is a summary of the important announcements in the Budget and the effects these may have on your personal and business taxation affairs

Personal Tax Rates

Low Income Tax Offset

Currently, the low income tax offset (LITO) is $1,200. Taxpayers eligible for the full LITO do not pay income tax until their annual income exceeds $14,000. From 1 July 2009 the LITO will increase from $1,200 to $1,350, meaning the effective tax free threshold will increase to $15,000. From 1 July 2010, the LITO will increase from $1,350 to $1,500, meaning the effective tax free threshold will increase to $16,000

Senior Australians Tax Offset

As a consequence of the changes in the low income tax offset, the tax free income threshold for eligible senior Australians will also change. Currently, eligible senior Australians have no tax liability until their incomes reach $28,867 for singles and $24,680 for each member of a couple. With the changes to the senior Australians' tax offset, eligible senior Australians will have no tax liability until their incomes reach:
-$29,867 for singles and $25,680 for each member of a couple in the 2009-10 income year; and
-$30,685 for singles and $26,680 for each member of a couple in the 2010-11 income year.

Private Health Insurance Rebate and Surcharge Changes

The Budget contained the much anticipated measures to scale back the private health insurance rebate for individuals with higher earning capacities.

From 1 July 2010, the Government will introduce three new "Private Health Insurance Tiers". These are as follows:

Tier 1: for singles earning more than $75,001 (couples $150,001), the Private Health Insurance Rebate will be 20%, for those up to 65 years (25% for those over 65, and 30% for those over 70 years). The Surcharge for avoiding private health insurance will remain at 1%.

Tier 2: for singles earning more than $90,001 (couples $180,001), the Private Health Insurance Rebate will be 10%, for those up to 65 years (15% for those over 65, and 20% for those over 70 years). The Surcharge for avoiding private health insurance will be increased to 1.25%.

Tier 3: for singles earning more than $120,001 (couples $240,001), no Private Health Insurance Rebate will be provided. The Surcharge for avoiding private health insurance will be increased to 1.5%.

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All income thresholds will continue to remain indexed to wages. For low and middle-income earners, the existing 30, 35 & 40% Private Health Insurance rebates will remain in place.

Personal Income Tax – Medicare Levy Low Income Threshold

From 1 July 2008, the Government will increase the Medicare levy low-income thresholds to $17,794 for individuals (up from $17,309 for the 2007/08 income year) and $30,025 for individuals in families (up from $29,207 for the 2007/08 income year).

The additional amount of threshold for each dependent child or student will also increase to $2,757 (up from $2,682 for the 2007/08 income year).

The Medicare levy threshold for pensioners below Age Pension age will also be increased to $25,299, with effect from 1 July 2008 (up from $22,922 for the 2007/08 income year). This increase will ensure that pensioners below Age Pension age do not pay the Medicare levy when they do not have an income tax liability.

Superannuation

Concessional Contribution Threshold Reduction

From 1 July 2009, the concessional contributions cap will be reduced from $50,000pa to $25,000pa. This cap will be indexed. The transitional cap for people over 50 years old will reduce from $100,000 to $50,000, with a further reduction to $25,000 at 1 July 2012 (or equivalent indexed amount at that time).

Non-concessional Contribution Threshold

This remains at $150,000 (scheduled to increase to $165,000 at 1 July 2009). It will be indexed in line with the concessional contributions cap and will remain at six times that cap.

Minimum Pension Withdrawal Reduction

The account based minimum pension withdrawal requirements will continue to be halved for 2009/10. This is an extension of the initiative announced earlier this calendar year. This measure assists self-funded retirees by not forcing a sale of assets at reduced market values and allowing the capital base to be invested for the future.

Co-Contribution Temporary Reduction

The co-contribution will be temporarily reduced. Non-concessional contributions of up to $1,000 are currently matched by the Government with a co-contribution of $1,500 for people earning less than $30,342. The co-contribution will be phased out up to an income level of $60,342. The co-contribution will reduce to $1,000 in 2009/10, 2010/11 and 2011/12 and increase to $1,250 in 2012/13 and 2013/14. It is scheduled to return to the full $1,500 in 2014/15 and future years.

Lost Superannuation Accounts

Superannuation accounts with less than $200 and accounts that have been inactive for more than five years with insufficient information to determine the owner will be paid to unclaimed monies from 1 July 2010.

Trans-Tasman Retirement Savings Portability

This proposed scheme will enable the transfer between certain Australian superannuation funds to KiwiSaver accounts. A memorandum of understanding is in place between the Australian and New Zealand Governments and more details with be forthcoming.

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Small Business

Increase in Investment Allowance for Small Business

Small business entities will be able to claim an increased investment allowance of 50% (instead of the previously announced 30%) of the cost of eligible assets acquired between 13 December 2008 and 31 December 2009, and installed by 31 December 2010. All other businesses will continue to access the investment allowance at 30% for eligible assets contracted for between 13 December 2008 and 30 June 2009, and 10% for eligible assets committed to investing in between 1 July 2009 and 31 December 2009, and installed by 31 December 2010. Small business entities need to invest a minimum of $1,000 on an individual asset in order to qualify for the 50% investment allowance.

Aggregation of Identical Assets

The Government reiterated that taxpayers will also be allowed to aggregate the eligible expenditure on identical or substantially identical assets to meet the requisite investment threshold. The eligible expenditure on assets may also be aggregated if they form part of a set. Items may be regarded as a set if they are dependent on each other, marketed as a set, or designed and intended to be used together.

Pay As You Go (PAYG) Instalments — Cash Flow Relief for Small Business

The Government will provide cash flow relief for small business by reducing Pay As You Go (PAYG) instalments for the 2009/10 income year for all taxpayers who pay quarterly PAYG instalments based on their previous year's tax adjusted by GDP growth. For the 2009/10 income year, the Government will reduce the GDP adjustment factor for calculating quarterly instalments under the GDP adjustment method from around 9% to 2%. This aligns the GDP adjustment rate with the expected consumer price index (CPI) for 2009/10 as forecasted. This measure was previously announced in a joint press release issued on 28 March 2009 by the Treasurer and the Minister for Small Business, Independent Contractors and the Service Economy.

Capital Gains Tax – Further Amendments to Small Business Concessions

The Government will make several changes to the small business capital gains tax (CGT) provisions so that they operate flexibly. A transitional rule will extend the time for taxpayers to choose to access the concessions where the choice arises from changes to the concessions announced in the 2008/09 Budget and the 2008/09 Mid-Year Economic and Fiscal Outlook. This extension of time will apply from Royal Assent of the amending legislation.

Access to the concessions for assets acquired on the death of an individual will be extended to cover assets that have passed to a testamentary trust where the individual would have been able to access the concessions at the time of their death. This extension will apply to CGT events happening in the 2006/07 income year and later income years.

The provisions which treat certain distributions to entities connected with a private company as dividends will be excluded from applying to the small business CGT retirement exemption. This exclusion will apply from Royal Assent of the amending legislation. This measure was introduced into Parliament together with the previously announced changes to the concessions on 19 March 2009.

Entrepreneurs' Tax Offset – Income Testing Deferred

The family income test for the entrepreneurs' tax offset which was announced in the 2008/09 Federal Budget will be deferred for a further 12 months.

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This means the family income test will commence on 1 July 2009 instead of 1 July 2008. The entrepreneurs' tax offset provides a maximum 25% tax offset against the tax liability for small business entities with annual turnover below $75,000. Under the proposed family income test, the entrepreneurs' tax offset would begin to be phased out for singles with income of $70,000 and families with income of $120,000. The deferral of the income test will mean eligible small business will not have their entrepreneur's tax offset reduced in the 2008/09 year.

Trusts

Capital Gains Tax - Reintroduction of Trust Cloning for Fixed Trusts

The Government recently announced changes to the tax law to eliminate CGT concessions for cloned trusts. However, the Government has now announced a limited CGT rollover for assets transferred between trusts that have the same beneficiaries with the same entitlements and no material discretionary elements (that is, fixed trusts). These amendments will apply to CGT events happening after 31 October 2008, that is, they will have effect from 1 November 2008.

Trustees of eligible trusts will be able to defer the CGT consequences of the asset transfer until the receiving trust subsequently deals with the asset. This will allow eligible trusts to restructure without immediate CGT consequences.

Without this Budget concession, the transfer of assets from one trust to another would trigger a CGT taxing point. This measure will be accompanied by appropriate integrity rules. For example, beneficiaries of the trusts will be required to adjust the CGT attributes of their interest(s) in the trusts to take account of the transfer. The abolition of the trust cloning exception and the CGT rollover for fixed trusts will be combined into one set of amendments.

Legislation giving effect to these measures will be introduced as soon as practicable. An exposure draft of the legislation will be released for consultation in the coming weeks on the Treasury website.

Closely Held Trusts

The Government will extend the application of the tax file number and withholding tax provisions to closely held trusts (including family trusts). As closely held trusts currently operate, where a beneficiary is presently entitled to trust income (and the trustee is not taxed on the distribution), the beneficiary is not required to provide a tax file number to the trustee prior to receiving the distribution. The beneficiary is then required to include the distribution in their income tax return.

Under new rules to take effect from 1 July 2010, all distributions from closely held trusts and family trusts will be subject to the tax file number and withholding tax provisions. Beneficiaries who are presently entitled to a distribution from any of these trusts will be required to provide the trustee with their tax file number.

Where the beneficiary fails to provide the trustee with a tax file number, the trustee will be required to withhold tax from the distribution at the rate of 46.5% (and remit this amount to the Australian Taxation Office). The beneficiary will receive the net amount of the distribution and be entitled to claim a tax offset for the tax withheld by the trustee. The offset is refundable, and the beneficiary will be entitled to a refund for any excess taxes withheld by the trustee. There will be no requirement for trustees to obtain tax file numbers from beneficiaries where the trustee is already subject to tax on the distribution, such as where the beneficiary is a minor.

Contact Us

For much more information about this year's budget changes including employment taxes, managed funds, corporate tax and R&D grants, contact us.

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