

Federal Budget Newsletter 2011-12

Key initiatives:

- ❖ Personal Income Tax Rates – including flood levy
- ❖ Minors no longer entitled to low income tax offset on unearned income
- ❖ Anstis overruled - No deductions against Government Assistance Payments
- ❖ Dependent spouse rebate for spouses under 40 to be phased out
- ❖ Medicare levy thresholds increased for 2010-11
- ❖ Income test on private health insurance rebate
- ❖ Support for low income earners
- ❖ HECS: reduction in discounts
- ❖ Family Tax Benefit, Baby Bonus & related changes
- ❖ Tax-free apprenticeship payments
- ❖ Excess contributions tax: refund option for contributions up to \$10,000.
- ❖ Changes to the Education Tax Refund
- ❖ Small Business motor vehicle write-off to replace Entrepreneur's Tax Offset
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- ❖ Income Tax Cuts



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Personal Tax Rates Including Flood Levy

The Government did not make any changes to the currently legislated tax rates which apply for the 2010-11 and following years (not forgetting that, from 1 July **2011** for one year, those rates will include the flood levy, where applicable). The resident tax rates are as follows:

Residents: rates and tax payable: 2010-11 and later years	
Taxable income (\$)	Tax payable (\$)
0 - 6,000	Nil
6,001 - 37,000	Nil + 15% of excess over 6,000
37,001 - 80,000	4,650 + 30% of excess over 37,000
80,001 - 180,000	17,550 + 37% of excess over 80,000
180,001 +	54,550 + 45% of excess over 180,000

Notes:

1. The above rates exclude the 1.5% Medicare levy and the flood levy (see below).
2. The low income tax offset is a maximum of \$1,500.

The current resident tax thresholds and those applying for the 2011-12 financial year (for those subject to the flood levy) are:

Tax threshold levels - flood levy comparison			
Current, and from 1 July 2011 for those NOT subject to the flood levy		2011-12 (for those subject to the flood levy)	
Taxable income (\$)	Rate (%)	Taxable income (\$)	Rate (%)
0 - 6,000	0	0 - 6,000	0
6,001 - 37,000	15	6,001 - 37,000	15
37,001 - 80,000	30	37,001 - 50,000	30
80,001 - 180,000	37	50,001 - 80,000	30.5
180,001 +	45	80,001 - 100,000	37.5
		100,001 - 180,000	38
		180,001 +	46

Note: The rates above exclude Medicare levy.

Flood levy

Generally, the flood levy will apply to individual taxpayers, both resident and non-resident, who have a taxable income over \$50,000 in the 2011-12 financial year. By virtue of the levy, for the 2011-12 financial year, the effective top personal marginal tax rate will be 47.5%, including the flood levy and the Medicare levy.

Under the levy:

- individuals with a taxable income between \$50,001 and \$100,000 will pay a 0.5% levy on that part of taxable income above \$50,000;
- individuals with a taxable income of \$100,001 or more will pay a 0.5% levy on that part of their taxable income between \$50,001 and \$100,000 and a 1% levy on that part of their taxable income above \$100,000; and
- no levy is payable where the taxpayer has a taxable income of \$50,000 or less, or where they fall into an exemption category as specified in a legislative instrument that is made by the Minister.

Exemption: Individuals are exempt from the levy if they were affected by a natural disaster during 2010-11 and received an Australian Government Disaster Recovery Payment. Where a trustee has income that is taxed as if the income was of an individual, they will be liable for the levy as per the relevant thresholds.

Obviously, the flood levy will mean an increase in tax rates for many people after 1 July **2011**. With the change (usually reduction) in tax rates that has taken place over recent years, traditional year-end tax planning has suggested that taxpayers, where possible, defer income and bring forward deductions. But this year, the reverse applies - although it is acknowledged that the increase in tax rates will be only small. For example, salary sacrificing into superannuation (within the limits that apply) after 1 July will reduce taxable income for that year and thereby reduce the impact of the flood levy.

The levy is calculated as follows:

Flood levy calculation	
Taxable income (TI) 2011-12 financial year (\$)	Flood levy (\$)
0 - 50,000	Nil
50,001 - 100,000	$[TI - 50,000] \times 0.5\%$
100,001 +	$250 + [(TI - 100,000) \times 1\%]$

Non-resident individuals

The tax rates for non-residents have not changed and are as follows:

Non-residents: rates and tax payable: 2010-11 and later years	
Taxable income (\$)	Tax payable (\$)
0 - 37,000	29%
37,001 - 80,000	10,730 + 30% of excess over 37,000
80,001 - 180,000	23,630 + 37% of excess over 80,000
180,001 +	60,630 + 45% of excess over 180,000

Note: The above rates exclude the 1.5% Medicare levy and the flood levy (the flood levy can apply to non-residents where they have taxable Australian income over \$50,000).

Minors No Longer Entitled to Low Income Tax Offset on Unearned Income

The Government will remove the ability of minors (children under 18 years of age) to access the low income tax offset (LITO) to reduce tax payable on their **unearned income**, such as dividends, interest, rent, royalties and other income from property, **with effect from 1 July 2011**. This is designed to discourage income splitting between adults and children, the Government said.

The Assistant Treasurer said the increases in LITO over recent years have increased the amount of income that can be allocated to children tax-free. He said these increases have been accompanied by increased distributions of income to children, especially from discretionary trusts.

Income earned by minors from work will still be eligible for the full benefit of the LITO. Unearned income of minors who are orphans or disabled, as well as compensation payments and inheritances received by minors, will not be affected by this measure.

Anstis Overruled – No Deductions Against Government Assistance Payments

The Government will amend the tax law to **prevent deductions being claimed against all government assistance payments, with effect from 1 July 2011**, in response to the 2010 High Court decision in *FCT v Anstis* [2010] HCA 40. The Government says the change is designed to maintain the integrity of the deductions system and provide certainty as to the scope of eligible deductions.

Commencing the denial of deductions from 1 July **2011** is designed to allow individuals who receive Youth Allowance (Student) to claim a deduction for expenses incurred in gaining their payment for the 2010-11 income year. This is to ensure individuals who have maintained records of their expenditure following the High Court decision are not precluded from claiming a deduction. For each of the years 2006-07 to 2009-10, the Commissioner of Taxation has determined that he will administer the law to allow eligible taxpayers to receive an automatic deduction of \$550 or make potentially higher claims if expenses can be substantiated.

Dependent Spouse Rebate for Spouses Under 40 to be phased out

The Government announced it will phase out the tax offset for dependent spouses aged less than 40 (ie born on or after 1 July 1971) "to help encourage more Australians into paid employment". This change will mean taxpayers with a dependent spouse aged less than 40 years will no longer be eligible for the dependent spouse tax offset (DSTO) from 1 July **2011**.

Exceptions: The change will not affect taxpayers whose dependent spouse is a carer, who is an invalid, or permanently unable to work; and taxpayers with children (eligible for Family Tax Benefit B), or eligible for the zone, overseas forces or overseas civilian tax offsets. Dependent spouses with children are not affected by this measure because they receive Family Tax Benefit B rather than the DSTO.

The Government says this change recognises that dependent spouses who may have been out of the paid workforce for many decades would find it more difficult to find jobs, so they will continue to be eligible for the DSTO.

The Treasurer said the offset had its origins in the initial ITAA 1936 at a time when a breadwinner was expected to "maintain" a spouse even without children, and there were limited employment opportunities for women. Mr Swan said this was no longer the case "for most Australians in today's modern economy, especially with unemployment set to fall further to 4.5%".

Medicare Levy Thresholds Increased for 2010-11

From the 2010-11 income year, the Medicare levy low-income thresholds will be increased for singles to \$18,839 (up from \$18,488 for 2009-10) and to \$31,789 for those who are members of a family (up from \$31,196 for 2009-10).

The additional amount of threshold for each dependent child or student will also be increased to \$2,919 (from \$2,865).

The Medicare levy low-income threshold for pensioners below Age Pension age will also be increased from 1 July 2010 to \$30,439 (from \$27,697). This increase will ensure that pensioners below Age Pension age do not pay the Medicare levy while they do not have an income tax liability.

Income Test on the Private Health Insurance Rebate

Although not formally announced in the **Budget**, Thomson Reuters confirmed with Treasury officials in Canberra that the Government plans to re-introduce a package of Bills (possibly in the **Budget** session) to income test the 30% private health insurance rebate. The measures will be essentially the same as the Bills that were defeated in the Senate in February and March 2010, although it is understood the threshold levels will be indexed upwards (as originally proposed).

The *Fairer Private Health Insurance Incentives Bill 2009*, *Fairer Private Health Insurance Incentives (Medicare Levy Surcharge) Bill 2009*, and *Fairer Private Health Insurance Incentives (Medicare Levy Surcharge - Fringe Benefits) Bill 2009* were originally introduced on 27 May 2009, and sought to give effect to 2009 **Budget** changes concerning the private health insurance rebate and consequential Medicare Levy Surcharge changes: see 2009 WTB 22 [1012].

The Bills were passed by the House of Reps without amendment, but were then defeated in the Senate in 2009 (see 2009 WTB 38 [1793]). They were re-introduced as [No 2] Bills on 19 November 2009 (see 2009 WTB 48 [2282]). The reintroduced Bills were then defeated in the Senate in February and March 2010: see 2010 WTB 10 [408].

The essence of the proposed changes was to effectively income test the private health insurance rebate. The Fairer Private Health Insurance Incentives Bill 2009 [No 2] proposed to introduce 3 new "Private Health Insurance Incentive Tiers":

- **Tier 1:** Singles earning between \$75,001 and \$90,000 and couples/families earning between \$150,001 and \$180,000 would receive a 20% private health insurance rebate if they are aged up to 65 years (25% if they are aged over 65, and 30% if they are aged 70 years or over).
- **Tier 2:** Singles earning between \$90,001 and \$120,000 and couples/families earning between \$180,001 and \$240,000 would receive a 10% private health insurance rebate if they are aged up to 65 years (15% if they are aged over 65, and 20% if they are aged 70 years or over).
- **Tier 3:** Singles earning above \$120,000 and couples/families earning above \$240,000 would not receive any private health insurance rebate, regardless of age.

The defeated Bills had also proposed to increase the rate of Medicare levy surcharge that certain taxpayers would be liable for when they have income for surcharge purposes above specified thresholds and do not have complying health insurance:

- Singles earning between \$90,001 and \$120,000 and couples/families earning between \$180,001 and \$240,000 would have been liable for a 1.25% Medicare levy surcharge.
- Singles earning above \$120,000 and couples/families earning above \$240,000 would have been liable for a 1.5% Medicare levy surcharge.

The fate of the Bills will probably rest with the Independents in the House of Reps, as the Greens have previously stated they are opposed to the private health insurance rebate, so it could be expected that any re-introduced Bills may obtain Greens approval in the Senate (especially if the Bills are debated in the Senate after 1 July **2011**).

Support for Low Income Earners

Payment of the Low Income Tax Offset (LITO) will be brought forward to deliver more timely assistance to households during the year, improving the immediate rewards for work and helping with cost of living pressures.

Currently, half of the LITO is delivered to workers during the year through pay as you go (PAYG) withholding, with the rest delivered later in their tax return. From 1 July 2011, 70 per cent of LITO will be paid when workers need it — reducing the tax workers pay through the year.

The LITO benefits low and middle income earners. Workers with income of \$30,000 will get an extra \$300 during the year in their regular pay. Workers with income of \$50,000 will get an extra \$140 during the year.

HECS: Reductions in Discounts

The Government will reduce the following discounts applying to payments made under the Higher Education Contribution Scheme (HECS):

- the discount available to students electing to pay their student contribution up-front will be reduced from 20% to 10%; and
- the bonus on voluntary payments to the Tax Office of \$500 or more will be reduced from 10% to 5%.

Under HECS, students electing to pay their student contribution up-front will continue to receive a 10% discount on the payment. Students choosing not to pay up-front can take out a concessional loan to pay their student contribution under the Higher Education Loan Program (HELP).

Under HELP, students accrue an outstanding debt which is repaid gradually when their assessable income exceeds a minimum repayment threshold. Students can also elect to make additional voluntary payments through the Tax Office to further reduce their outstanding HELP debt. Payments of \$500 or more will now attract a 5% bonus so that a payment of \$500 would reduce an individual's outstanding HELP debt by \$525.

Family Tax Benefit, Baby Bonus and Related Changes

The 2011-12 **Federal Budget** provides an increase in Family Tax Benefit (FTB) Part A for 16-19 year olds.

From 1 January 2012, the new maximum rate of FTB Part A for 16-17 year olds in secondary school will be increased from the current \$52.64 per fortnight to \$214.06 per fortnight, ie by around \$160 per fortnight - an increase of around \$4,200 per year. For 18-19 year olds in school, the rate will be \$3,741 per year. This will align with the 13-15 year old rate and ensure assistance for families does not drop when children turn 16. The increases to FTB Part A will only be available for families where their teenager is in full-time secondary study, or the vocational equivalent.

From 1 January 2012, the Government will lower the maximum age of eligibility for FTB Pt A from 24 to 21. This will bring FTB Pt A into line with the reduction in the Youth Allowance age of independence to 22 from 1 January 2012.

From 1 July **2011**, families will be able to advance a maximum of 7.5% of their total rate of FTB Pt A payment, up to \$1,000. For example, a family with 2 children under 12 will be able to receive an advance payment of up to \$644.

The Government also said it would extend indexation pauses on higher income limits for a further 2 years until 30 June 2014 in the following areas:

- the FTB Pt B primary earner income limit will remain at \$150,000;
- the income limit for receiving dependency tax offsets will remain at \$150,000;
- the Baby Bonus eligibility limit will remain at \$75,000 family income in the 6 months following the birth or adoption of a child;
- the Paid Parental Leave income limit will stay at \$150,000 for the primary carer in the previous financial year before the birth of the child;
- the higher income-free area of FTB Pt A will remain constant.

Fortnightly payment rates for Family Tax Benefit and the Baby Bonus will continue to be indexed every year.

The annual end of year FTB supplements will be held at the current levels for the next 3 years. The FTB supplements will be fixed at the current 2010-11 levels of \$726.35 per annum per child for FTB Pt A and \$354.05 per annum for FTB Pt B until 1 July 2014.

Tax-free Apprenticeship Payments

The 2011-12 **Budget** includes \$281m for additional tax-free payments to encourage apprentices in critical trades to complete their qualifications. The Government expects the \$1,700 Trades Apprentice Income Bonus to support 200,000 trade apprentices over 4 years in skills shortage occupations to stay in their training and get a skilled job.

From 1 January **2011**, eligible Australian Apprentices have received an additional tax-exempt bonus of up to \$1,700 as they reach milestones in their training, including an \$800 completion bonus, bringing them to a total of a maximum of \$5,500 over the course of their apprenticeship.

The incentive payments were announced in the 2010 Election as part of a package to support Australian Apprentices and as at May **2011**, the PM said more than 34,000 Australian Apprentices had already benefited from this new payment.

Excess Contributions Tax: Refund Option for Contributions up to \$10,000

The Government will provide eligible individuals who breach the concessional contributions cap by up to \$10,000 with a one-off option to request that these excess contributions be refunded to them. This new refund option will only apply to first time breaches from 1 July **2011**.

The changes will give individuals the option to take excess concessional contributions out of their superannuation fund and have them assessed as income at their marginal rate of tax, rather than the excess concessional contributions tax rate of 31.5% (in addition to the 15% contributions tax for the fund).

The Government expects that this reform will help to reduce the number of occasions where the concessional contributions are exceeded resulting in an excess contributions tax (ECT) assessment.

The Government said it will consult with the superannuation industry on the implementation of this measure.

Concessional contributions

Concessional contributions generally include employer contributions (those made under salary sacrifice arrangements and super guarantee contributions) and personal contributions for which the taxpayer intends to claim a deduction. However, less obvious concessional contributions include notional taxed contributions for defined benefit interests, transfers of certain fund reserves and payments by employers of fund expenses (eg life insurance premiums).

Since 2009-10, the "concessional contributions cap" has been set at \$25,000 (or \$50,000 for those aged 50-74 until 30 June 2012). Note that the Government has proposed to allow individuals aged 50 and over with less than \$500,000 in super to contribute \$25,000 more per year than other individuals from 1 July 2012, when the general concessional contributions cap increases with indexation from \$25,000 to \$30,000, the higher cap will increase by the same dollar amount.

Date of effect

This measure will apply from 1 July **2011** in respect of 2011-12 or later years, and only for the first year, commencing from 2011-12, in which a breach occurs.

Obviously, this reform may benefit taxpayers with a marginal rate below the top marginal rate of 46.5% who inadvertently breach the concessional contributions cap by \$10,000 or less for the first time. The reform will also provide some one-off relief in situations where excess concessional contributions (up to \$10,000) would otherwise flow through and also result in a breach of the non-concessional contributions cap and trigger a tax rate up to 93%.

Unfortunately, the one-off nature of the measure will only provide partial relief where a taxpayer may have repeated the error over a couple of financial years. Due to the time lag for the Commissioner to collect and process contributions data to notify a taxpayer about a potential cap breach, it may be a couple of years before a taxpayer becomes aware of a problem. In addition, the measure will not provide any relief for taxpayers who inadvertently exceed the concessional cap by more than \$10,000 or for breaches before 1 July **2011**. Such taxpayers will need to apply to the Commissioner to disregard or reallocate the excess contributions.

Changes to the Education Tax Refund

The ETR assists parents and carers with expenses such as computers, stationery and textbooks which can place pressure on the family budget. The Government is extending the ETR, at an estimated cost of \$460 million over four years, to cover school uniforms, including optional uniforms and sports uniforms.

Small Business Motor Vehicle Tax Write-off to Replace Entrepreneur's Tax Offset

The Government will provide Australian small businesses with an instant tax write-off of the first \$5,000 of any motor vehicle purchased from 2012-13. The Treasurer said that, for example, a tradesman on a 30% marginal tax rate, buying a new \$33,960 ute would receive an extra tax benefit of \$1,275 in the year they purchased the vehicle. The remainder of the purchase value can be transferred into the general small business depreciation pool, which is depreciated at 15% in the first year and 30% in later years.

The Treasurer said this new write-off was in addition to the Government's proposed tax reforms for small businesses to be introduced in 2012-13 that would allow:

- an immediate write-off of all assets valued at under \$5,000 (up from \$1,000 presently);
- a write-off of all other assets (except buildings) in a single depreciation pool at a rate of 30%. Currently, small businesses allocate assets to 2 different depreciation pools, with 2 different depreciation rates (30% and 5%); and
- a reduction in company tax rate to 29% for incorporated small businesses.

These reforms will be available to all small businesses, including sole traders and businesses operating through trusts, partnerships and companies. These tax reforms were originally announced as part of the Government's response to the Henry Tax System Review report in May 2010 and there has so far been no legislation introduced to implement them.

The new small business instant write-off for the first \$5,000 of any motor vehicle will effectively replace the Entrepreneurs Tax Offset (ETO), which will be abolished with effect from the 2012-13 income year. The Henry Tax System Review recommended abolition of the ETO because of its poor targeting and high compliance costs. The Henry Report concluded that ETO provided a disincentive for businesses to grow because the benefit available started to decline at \$50,000 of annual turnover and cut out completely at \$75,000. The ETO was also only available to individuals with incomes under \$70,000 and the Government said its poor targeting and complexity meant 2.3m small businesses missed out on any benefit.

While the \$5,000 deduction will be welcome for many small businesses, those with cash flow issues may find it difficult to outlay the initial funds to secure the deduction.

FBT and Cars – Flat 20% Valuation Rate to Apply

The Government announced what would amount to implementation of Henry Tax Review Recommendation 9(c) that the current statutory formula 4-percentage rate scale method for valuing car fringe benefits be replaced with a single statutory rate of 20%, regardless of the number of kilometres travelled.

Date of effect

The changes will apply to new vehicle contracts entered into after 7:30pm (AEST) on 10 May 2011, and will be phased in over 4 years as follows:

FBT statutory rate method					
	Statutory rate (x cost of car to determine person's car fringe benefit)				
Distance travelled during FBT year (1 April - 31 March)	Existing contracts (%)	New contracts from 10 May 2011 (%)	New contracts from 1 April 2012 (%)	New contracts from 1 April 2013 (%)	New contracts from 1 April 2014 (%)
0 - 15,000km	26	20	20	20	20
15,000 - 24,999km	20	20	20	20	20
25,000km - 40,000km	11	14	17	20	20
More than 40,000km	7	10	13	17	20

People who use their vehicle for a significant amount of work-related travel will still be able to use the "operating cost" (or "log book") method to ensure their car fringe benefit excludes any business use of the vehicle.

The change may encourage employers and employees to:

- purchase lower cost and more fuel efficient cars.
- keep company cars longer
- investigate more use of cars with diesel engines
- encourage more employee contributions to reduce the FBT liability.

Win for Teachers

Promoting high performance in teaching

Research shows that quality teaching is the single most important school based contributor to student achievement. This Budget invests \$872 million in our schools and delivers on two election commitments to continue the Government's support for high quality teaching.

Rewarding our great teachers

The *National Rewards for Great Teachers* program will provide \$425 million over the next four years, with \$125 million each semester from 2014, to reward top performing teachers with a bonus of up to 10 per cent of their salary.

New pathways into teaching

The Teach Next initiative will invest \$18.1 million to provide a new pathway into a teaching career for professionals with specialist qualifications or relevant experience to enhance the diversity of the teaching workforce and to promote 'real-world' links in the classroom.

Income Tax Cuts

	2008-09	2009-10	2010-11	2011-12	Total annual income tax benefit compared to 2007-08	Total income tax benefit as % of tax paid (including ML) in 2007-08
Taxable Income (\$)	Income Tax Cuts (\$)	Income Tax Cuts (\$)	Income Tax Cuts (\$)	Temporary Flood and Cyclone Reconstruction Levy (\$)	(\$)	
15,000	450	150	-	0	600	100%
20,000	450	150	150	0	750	46%
25,000	450	150	150	0	750	30%
30,000	450	150	150	0	750	23%
35,000	1,050	300	150	0	1,500	30%
40,000	1,050	300	450	0	1,800	26%
45,000	1,050	300	450	0	1,800	21%
50,000	1,000	300	450	0	1,750	17%
55,000	800	300	450	-25	1,525	13%
60,000	600	300	450	-50	1,300	10%
65,000	600	150	400	-75	1,075	7%
70,000	600	150	300	-100	950	6%
75,000	600	150	300	-125	925	5%
80,000	1,100	150	300	-150	1,400	7%
85,000	1,100	250	350	-175	1,525	7%
90,000	1,100	350	400	-200	1,650	7%
95,000	1,100	450	450	-225	1,775	7%
100,000	1,100	550	500	-250	1,900	7%
110,000	1,100	750	600	-350	2,100	6%
120,000	1,100	950	700	-450	2,300	6%
130,000	1,100	1,150	800	-550	2,500	6%
140,000	1,100	1,350	900	-650	2,700	6%
150,000	1,100	1,550	1,000	-750	2,900	6%
160,000	1,600	1,750	1,100	-850	3,600	7%
170,000	2,100	1,950	1,200	-950	4,300	7%
180,000	2,600	2,150	1,300	-1,050	5,000	8%
190,000	2,600	2,150	1,300	-1,150	4,900	7%
200,000	2,600	2,150	1,300	-1,250	4,800	7%
250,000	2,600	2,150	1,300	-1,750	4,300	4%

Note: the temporary flood and cyclone reconstruction levy is included when calculating total changes in income tax payable since 2007-08.

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