Federal Budget Update 2012

Investor Version

BT Federal Budget Update 2012

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Budget 2012/13

1. Key Highlights

- Commitment to previously legislated personal tax cuts from 1 July 2012
- Deferral of higher concessional contribution threshold until 1 July 2014
- Introduction of higher tax on concessional super contributions for high income earners
- Removal of CGT discounting for non-resident individuals

2. Budget Overview 2012/13

On 8 May 2012, the Federal Government handed down its Budget for 2012/13.

It would be fair to say that everyone will be impacted in some way by the measures contained in the Budget itself, or by other recent announcements from the Government that will apply from 1 July 2012.

Many of the measures in the Budget had been released, leaked or alluded to in the days leading up to the Budget itself, so there weren't a lot of hidden surprises. However, one major surprise was the Government's decision to defer the (re)introduction of a higher concessional contribution threshold for people aged 50 or over to 1 July 2014. Previous announcements have indicated a 1 July 2012 start date.

This deferral announcement, along with many other measures released, does highlight the need to establish and have an on-going relationship with a financial planner. Whilst everyone is likely to be impacted by the Budget announcements in some way, some will be impacted more. With a constantly changing legislative environment as the Government seeks to deliver a Budget surplus, there can be no substitute for receiving advice from your financial planner as to how these measures affect your personal circumstances, and to have someone to guide you through the changes.

Despite largely having been announced previously, most measures will still need legislation to be introduced, so the final version of the changes may differ to the announcements made in the Budget. As with all changes, it is important that you speak with your financial adviser to determine how these announcements will impact on your personal situation.

3. Market Reaction

A look at what this means for markets, from BT Financial Group's Chief Economist, Chris Caton.

Markets don't fuss nearly as much about Budgets as they used to do, and quite right too. None of the new policy measures seem to have dramatic equity market implications (if they did, the incessant pre-publication would mean that it's already priced in), and the debt projections only confirm what is widely known except for a few recalcitrant politicians and some ignorant agenda-pushing shock jocks; **Australia does not have a Government debt problem, and is in no danger of losing its AAA rating**. Given that the 10-year bond rate starts at less than 3.5%, this seems to be well recognized by markets.

The 2012/13 Budget was framed against an intriguing background; a Government in trouble and a two-speeded economy, both desperately seeking traction. In the past two Budgets, the Labor Government made a commitment to return to surplus in 2012/13. In the run-up to

Tuesday night, it repeated this commitment at length. So it is no surprise at all that the Budget for 2012/13 projects a wafer-thin surplus of $1.5 billion. Given that a substantial deficit will be recorded this year (the current estimate is $44.4 billion), this will be a massive fiscal turnaround if achieved, equivalent to just over 3% of GDP (see table below). Not only would it be unprecedented in Australia, it would have rarely happened elsewhere. At present, probably only Greece and New Zealand are engaging in fiscal tightening of the same magnitude.

For investors, there is little or no effect on the bond market. On equities, the handouts, particularly to low-income earners, should benefit retail, particularly supermarkets. The superannuation measures are unfavourable for the wealth managers. The deferral of the plan to reduce the tax on interest payments is unfavourable for the banks and, of course, affects investors directly. The decision not to proceed with the cut in the corporate tax rate may have a minor depressing effect on equities. As always, given the extent of leaks beforehand, some of this may already have been priced in.

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Key points on Superannuation

1. Additional 15% tax on superannuation contributions for high income earners

Effective Date of 1 July 2012

The Government confirmed the introduction of an additional 15% tax on concessional contributions made to superannuation for those earning income of more than $300,000pa.

The definition of income for this purpose includes:

- Taxable income
- Concessional contributions
- Adjusted fringe benefits
- Total net investment loss
- Target foreign income
- Tax-free Government pension and benefits
- **Less** child support payments

For the purpose of this additional tax, concessional contributions includes SG contributions, voluntary employer contributions, salary sacrifice contributions and personal deductible contributions. For defined benefit members, concessional contributions also include notional employer contributions to (funded and unfunded) defined benefit schemes.

The Government has advised that if a taxpayer's income exceeds $300,000 only due to their concessional contributions, the additional 15% tax will only apply to that portion of their contributions in excess of $300,000. For example, where income excluding concessional contributions is $285,000, and concessional contributions are $20,000 taking total income to $305,000, the additional tax will only apply on $5,000 of the concessional contributions.

The additional tax will not apply to excess contributions (those over the concessional contributions cap) as the individual has not received any tax concessions on these.

Treasury will consult with the superannuation industry and other relevant stakeholders on further design and implementation details.

The table below illustrates the impact of the additional 15% tax in a range of circumstances.

Salary (excluding Super)	**$280,000**	**$280,000**	**$300,000**	**$300,000**
Concessional contributions	**$25,000**	**$30,000**	**$25,000**	**$30,000**
Contributions tax at 15%	$3,750	$4,500	$3,750	$4,500
Additional 15% tax	$750	$1,500	$3,750	$3,750
Excess tax at 31.5%	$0	$1,575	$0	$1,575
Total Conts tax	**$4,500**	**$7,575**	**$7,500**	**$9,825**
Net Super contribution	**$20,500**	**$22,425**	**$17,500**	**$20,175**

2. Higher concessional contributions cap for those aged 50 years and over

Effective date of 1 July 2014

The existing transitional $50,000 concessional contributions cap for individuals who are aged 50 or over ends on 30 June 2012.

On 2 May 2010, the Government announced as part of the *Stronger, Fairer, Simpler: A Tax Plan for our Future* that from 1 July 2012, it would provide a higher concessional contributions cap for individuals aged 50 years or over with total superannuation balances below $500,000 from 1 July 2014.

The Government has reconfirmed their commitment to this measure but will defer the start date by two years, to 1 July 2014.

From 1 July 2014, individuals aged 50 and over with superannuation balances below $500,000 will be able to make up to $25,000 more in concessional contributions than allowed under the general concessional contributions cap.

This means for the 2012/13 and 2013/14 financial years, the general $25,000 concessional contributions cap will apply to all individuals.

> Whilst a doubling of the effective tax rate doesn't sound good, it's important to remember that a 30% tax rate on these contributions is still better than the 46.5% personal tax (including Medicare) that would otherwise be payable on this amount if not contributed to super.

3. Low income superannuation contribution (LISC)

Effective Date of 1 July 2012 (already legislated)

The LISC, will effectively return the amount of tax paid on concessional contributions to superannuation for eligible low income earners.

An individual will generally be eligible for LISC in a financial year if their adjusted taxable income[1] is not more than $37,000 and at least 10% of their total income[2] was sourced from employment.

The amount of LISC payable will be calculated as 15% of the total concessional contributions made by or on behalf of the individual for the financial year, up to a maximum of $500. Where the amount of LISC calculated is less than $20, no LISC will be paid on behalf of the individual.

The ATO will generally pay the LISC to a superannuation fund or RSA that holds an interest on behalf of the individual.

1_Adjusted taxable income = taxable income + adjusted fringe benefits + target foreign income + total net investment loss + tax-free pension or benefit + reportable superannuation contributions LESS deductible child maintenance expenditure.

2_Total income = assessable income + reportable fringe benefits + reportable employer superannuation contributions

4. Superannuation Guarantee (SG) Changes

Effective Date of 1 July 2013 (already legislated)

From 1 July 2013, the SG rate will gradually increase each financial year until it reaches 12% from 1 July 2019. The first increment in 2013/14 will bring the SG rate to 9.25%. The table below shows the SG rate applying for each financial year up to 2019/20.

Quarter during the income year	Charge percentage (%)
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 and subsequent income years	12

From 1 July 2013, the maximum age limit for receiving SG contributions (currently age 70) will also be abolished.

5. Tax relief for super fund mergers

Effective date of 1 June 2012 and 1 July 2013

The Government reconfirmed its intention to provide tax relief allowing superannuation funds to merge without triggering adverse tax consequences for members.

Given the potential benefits to members participating in superannuation fund mergers and successor fund transfers as well as the possible costs for superannuation funds transitioning to MySuper, the Government will provide:

- from 1 June 2012 to 1 July 2017, optional loss relief for mergers of complying superannuation funds on the same terms and conditions as the former temporary loss relief (which ceased 30 September 2011) with some exceptions including an optional roll-over for capital gains and proposed integrity provisions; and
- from 1 July 2013 to 1 July 2017, an optional roll-over and loss relief for capital gains and capital losses on mandatory transfers of default members' benefits and relevant assets to a MySuper product in another complying superannuation fund.

Self-managed superannuation funds will be excluded from the relief because the MySuper requirements do not apply to them.

A discussion paper on this tax relief will be released in the next few weeks.

Key points on Taxation

1. Reductions in Personal Income Tax

Effective from 1 July 2012

The Government has confirmed previously announced changes to the personal income tax rates and Low Income Tax Offset (LITO) to apply from 1 July 2012. These changes are aimed at delivering tax cuts to the low and middle income earners, ensuring assistance is received for the impact the carbon price will have on the cost of living. These changes have already been legislated.

Tax rates and thresholds for this and the next financial year are shown below:

Personal income tax rates					
2011/12			2012/13		
Income Threshold $	Marginal rate*	Tax on this income*	Income Threshold $	Marginal rate*	Tax on this income*
Up to 6,000	Nil	Nil	Up to **18,200**	Nil	Nil
6,001 – 37,000	15%	15c for each $1 over $6,000	**18,201** – 37,000	**19%**	**19c** for each $1 over **$18,200**
37,001 – 80,000	30%	$4,650 plus 30c for each $1 over $37,000	37,001 – 80,000	**32.5%**	**$3,572** plus **32.5c** for each $1 over $37,000
80,001 – 180,000	37%	$17,550 plus 37c for each $1 over $80,000	80,001 – 180,000	37%	**$17,547** plus 37c for each $1 over $80,000

180,001+	45%	$54,550 plus 45c for each $1 over $180,000	180,001+	45%	**$54,547** plus 45c for each $1 over $180,000

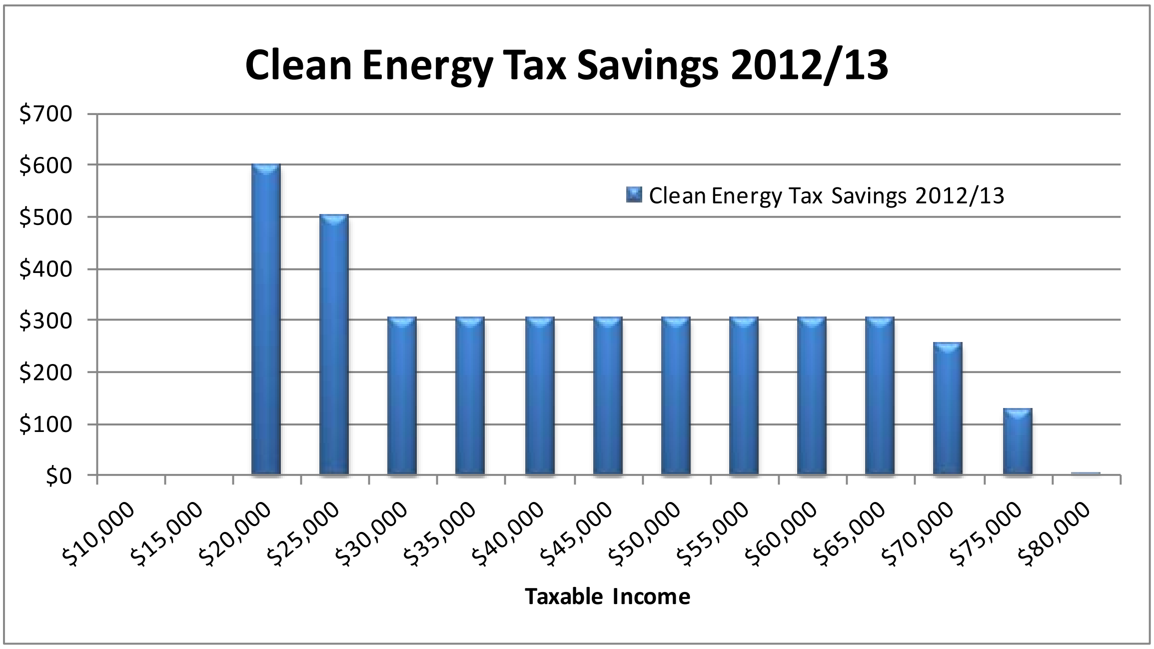
* These rates apply to Australia residents for taxation purposes and do not include the Medicare Levy of 1.5%.

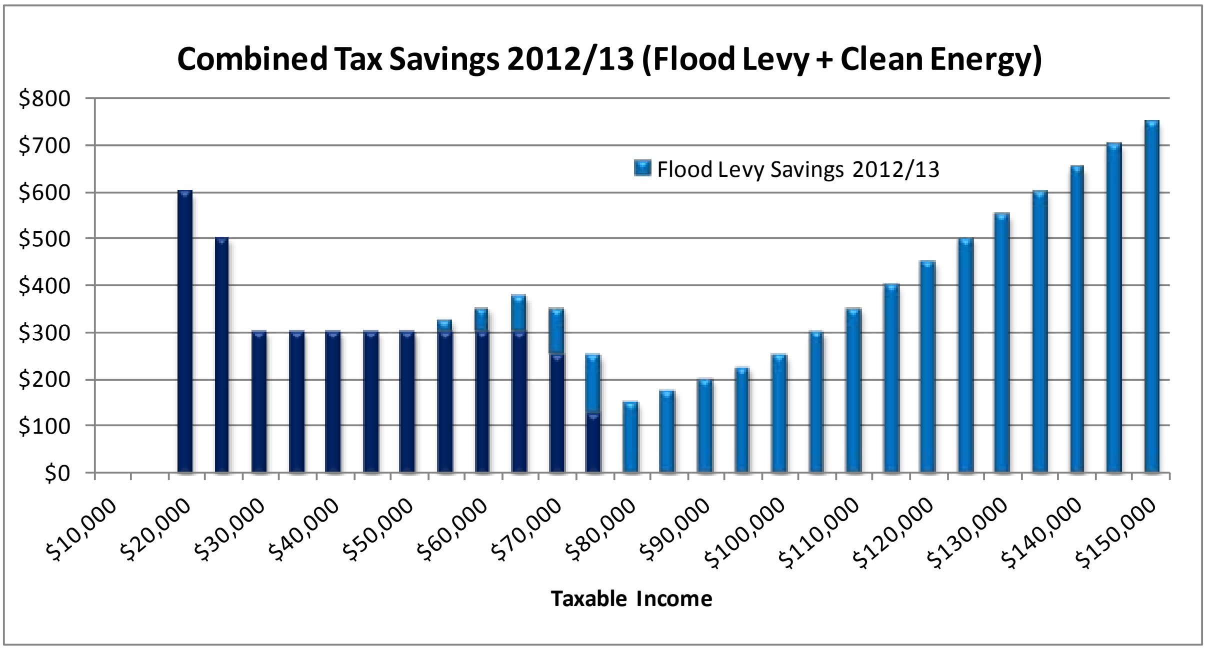
LITO will decrease from $1,500 to $445 for 2012/13, phasing out after $37,000 by 1.5 cents in the dollar to a maximum of $66,667 as per the below table. The impact of these changes are that the effective tax-free threshold will increase from $16,000 to $20,542 in 2012/13.

Additional changes will also come into effect from 1 July 2015 as follows:

- The tax-free threshold will increase to $19,400
- Marginal tax rate of between $37,001 and $80,000 will increase to 33% (or $3,344 plus 33c for each $1 over $37,000)
- The Low Income Tax Offset will further decrease to $300 with a phase out rate of 1% and an upper limit of $67,000.

The graphs below show the reduction in tax payable for the 2012/13 financial year as compared to the 2011/12 financial year for a range of taxable incomes.





2. Removal or reduction in Private Health Insurance rebate

Effective from 1 July 2012 (already legislated)

Whilst not raised in this year's Budget, it is important to be aware that from 1 July 2012 the existing Private Health Insurance rebate will be scaled back or removed for those earning $84,000 or above (singles) or at least $168,000 (couples), with an increase in the Medicare Levy Surcharge for those who opt out of private health insurance.

The level of rebate available or potential Medicare Levy Surcharge that could be imposed is set out in the following table.

Income		Level of rebate based on age			Medicare Levy Surcharge
Single	Couple	<65	65 to 69	70+	
<$84,000	<$168,000	30%	35%	40%	Nil
$84,000-$96,999	$168,000-$193,999	20%	25%	30%	1%
$97,000 - $129,999	$194,000 - $259,999	10%	15%	20%	1.25%
$130,000 +	$260,000 +	Nil	Nil	Nil	1.5%

As an example, if you earn more than $130,000 per annum, you will lose the current 30% private health insurance rebate. For every $1,000 of premium, this is an extra $300 that you will now have to pay. However, if you choose not to have the private health cover, at $130,000 of taxable income, the Medicare Levy Surcharge would equate to $1,950.

If your premium was $2,000, based on this example you may question the validity of owning this policy from a cost perspective. However, as with all insurance policies, whilst the premiums may sometimes seem out of reach, the real value of the policy will come through when something happens and you need to make a claim.

Most private health funds are offering the ability to pre-pay premiums for a 12 month period. If you take advantage of this and prepay your 2012/13 before 1 July 2012, you will still receive the full rebate as it is based on the time of payment.

3. Flood and cyclone reconstruction levy

Applicable for the year ended 30 June 2012

Effectively introduced in last year's Federal Budget, this levy applies only to the current financial year at a rate of up to 1% (for taxable income above $100,000). Individuals who received an Australian Government Disaster Recovery Payment (AGDRP) from Centrelink for certain natural disasters in 2010/11 were exempt from the payment of this levy.

That exemption has now been extended to:

- those eligible for that AGDRP but did not apply for it, and
- those eligible for an AGDRP for natural disasters in 2011/12, namely the floods in NSW and Queensland.

4. Changes to the taxation of employment termination payments

Effective from 1 July 2012

Concessional tax treatment that generally applies to employment termination payments (ETP) will be reduced from 1 July 2012. However, this measure is intended to only apply to "golden handshake" arrangements and not in cases where the payment has arisen as a result of a genuine redundancy (including to those 65 and over), invalidity, compensation due to an employment related dispute and death.

Under this measure, in addition to the existing ETP cap (which will be indexed to $175,000 from 1 July 2012) under which a component of an ETP is taxed at a maximum of 15% or 30% (depending on the individual's age), the ETP cap will only be available to the extent the ETP does not cause the individual's taxable income to exceed $180,000.

As an example, assume you receive an ETP in May 2013 for $100,000. Your other taxable income for the year is $150,000. If you still have your full ETP cap, the entire $100,000 (as it is below the ETP cap) would be taxed at a maximum rate of 15% (if you have reached your preservation age – currently 55) or 30% (if you are below your preservation age). Ignoring Medicare levy, this would result in a tax liability of $15,000 or $30,000.

Under this new measure, the concessional tax treatment is only available to the extent the $100,000 payment doesn't take you above $180,000 of taxable income. In this example, only the first $30,000 of the payment will be concessionally taxed (at 15% or 30%) and the balance of $70,000 will be taxed at your marginal rate (which as it takes you over the $180,000 threshold will be 45%). Your tax liability on the ETP will therefore be $36,000 or $40,500.

5. Net Medical Expense Tax Offset

Effective from 1 July 2012

The Government has announced it will introduce a means test for the net medical expenses tax offset (NMETO) whereby those with adjusted taxable income above the Medicare levy surcharge thresholds will only be able to claim medical expenses over a threshold of $5,000 instead of the current $2,060. Furthermore, the offset they may claim will be 10% of the expenses above the threshold instead of the current 20%.

The Medicare levy surcharge thresholds for 2012/13 are $84,000 for singles and $168,000 for couples or families.

6. Changes for non-resident taxpayers

From 8 May 2012

With effect from Budget night (ie from 8 May 2012), non-residents will no longer be able to access the standard 50% discount on assessable capital gains.

For non-residents, it is generally only real property located in Australia that is subject to the capital gains tax provisions, however it may have some application to former Australian tax residents who have since become non-resident and elected to defer the taxation of gains on assets they held (and still hold) prior to departing Australia. For example, this may include share and managed fund portfolios.

If you are a non-resident, you can can still be eligible for a 50% discount on the gain from the time of acquisition to 8 May 2012 (provided that period is greater than12 months) using a valuation of the affected asset as at 8 May 2012. However, any capital gain accruing after 8 May 2012 will be assessed in full.

If you are an Australian tax resident, but moving overseas and losing your tax residency status, it is important that you obtain advise on the CGT implications that may arise for you in the future.

From 1 July 2012

Under existing thresholds, non-residents do not receive a tax free threshold of $6,000 but are subject to tax from their first dollar of taxable income at the rate of 29% up to $37,000 of taxable income. Beyond that income, the marginal rates align to those applying to resident taxpayers.

From 1 July 2012, this lower threshold will be removed, and non-residents will pay tax at the rate of 32.5% on their taxable income up to $80,000 and thereafter at the same rates that apply to resident taxpayers. From 1 July 2015, the 32.5% will increase to 33% in line with that applicable to resident taxpayers.

7. Living away from home allowances (LAFHA)

Effective from 1 July 2012

Payments of a LAFHA generally can qualify for tax exempt treatment as well as concessional (or exempt) treatment for fringe benefits tax (FBT) purposes.

Subject to some exemptions, the Government has proposed to amend the FBT treatment and prevent misuse of the exemption by allowing non-residents to only access the benefit if they also maintain a home for their own use in Australia, which they are then living away from to qualify for the LAFHA. This change will essentially treat non-residents in the same manner as permanent residents. The concessional treatment of the LAFHA will also only be available for a maximum period of 12 months for an individual in any particular location (ie will prevent the concessions being indefinitely available).

8. Phase out of mature age worker tax offset

Effective from 1 July 2012

Under existing legislation, a person aged 55 or over is entitled to a mature age worker tax offset (MAWTO) of up to $500 if they have eligible "net working income" below $53,000 and a reduced amount on income up to $63,000.

From 1 July 2012, this offset will no longer be available to those born on or after 1 July 1957. This will impact those who have not yet qualified to receive the MAWTO based on their current age.

If you are currently eligible based on your age, you will continue to be eligible to receive this offset.

9. Company tax loss carry back

Effective 1 July 2012

From 1 July 2012, companies that generate a revenue loss (ie is not applicable to capital losses) in a particular income year will be able to carry that loss back up to two income years (only one year for losses arising in the year ended 30 June 2013 – the first year of operation). Where this occurs, the company will then be eligible for a refund of tax paid in those prior years, but will not have that loss available to carry forward into the future.

The amount of loss that can be carried back is capped at $1,000,000 of losses generated in a particular income year and will also be capped by reference to a company's franking account balance.

10. Abandonment of previously announced measures

The Government has announced that it will no longer proceed with certain measures announced in prior Budgets that had not yet come into effect including:

- The lowering of the company tax rate from its current 30% level to 29% (and 28% for small businesses)
- The standard deduction for work related expenses – previously announced to be a $500 deduction available from 1 July 2013 (and $1,000 from 1 July 2014)
- The 50% discount on the first $1,000 of interest income earned, which was due to come into effect from 1 July 2013.

Key points on Social Security

1. Schoolkids Bonus

Effective from 1 January 2013

The Government will replace the Education Tax Refund (ETR) with a Schoolkids Bonus to be paid as two equal instalments in January and July each year. Families in receipt of Family Tax Benefit Part A (FTB A) will be paid:

- $410 p.a. for each primary school student, and
- $820 p.a. for each secondary school student

All eligible families will receive the full rate of payment. As a result, families are no longer required to retain receipts as proof of purchase or wait until they submit their tax return.

2. Changes to Family Tax Benefit Part A

Effective from 1 July 2013

The Government will increase the maximum payment of FTB A by:-

- $300 p.a. for families with 1 child, and
- $600 p.a. for families with 2 or more children

For families receiving the base rate of FTB A, the increase will be:-

- $100 p.a. for families with 1 child, and
- $200 p.a. for families with 2 or more children

For example, a family with two children under the age of 12 will receive a $600 boost, up to a family adjusted taxable income of around $78,000 p.a. or a $200 boost, with a family adjusted taxable income between around $78,000 p.a. and around $112,000 p.a.

Additionally, the Government will tighten the age requirement for FTB A from less than 21 years of age, to less than 18 years of age (or where a young person remains in secondary school, the end of the calendar year in which they turn 19). Individuals who no longer qualify for FTB A may be eligible to receive Youth Allowance subject to usual eligibility requirements.

3. Australian Working Life Residency

Effective from 1 January 2014

Currently, Age Pension recipients who are overseas for more than 26 weeks are only paid their maximum entitlement if their Australia Working Life Residence (AWLR) is 25 years or more. A recipients AWLR refers to periods from age 16 to Age Pension age when they were an Australia resident. (There is no requirement to work to accrue AWLR years).

The Government will amend these rules so that the maximum entitlement will only continue if their AWLR is 35 years or more. Pension recipients with less than 35 years AWLR will be paid a proportional rate.

4. Portability of certain Australian Government Payments

Effective from 1 January 2013

The Government is tightening the rules for people who travel overseas while receiving certain income support and family assistance payments.

Under the change, the amount of time individuals can travel overseas while continuing to receive their payment will be reduced from 13 weeks to 6 weeks.

This measure affects the majority of Centrelink payment and benefits, but does not apply to the Age Pension.

5. Parenting Payment – tightening of eligibility for grandfathered recipients

Effective from 1 January 2013

Currently, recipients of Parenting Payment (PP) who were granted the payment prior to 1 July 2006 do not lose eligibility until their youngest child attains age 16.

The Government will align PP eligibility for all recipients so that the payment will cease when the youngest child attains age 6 (for partnered recipients), or age 8 (for single recipients).

6. Liquid Asset Waiting Period

Effective from 1 July 2013

The Government will increase the maximum reserve amount for the liquid assets waiting period for recipients of particular income support payments. Liquid assets are assets in the form of cash or those which can be easily converted into cash, including shares and term deposits. A single person without dependents will now have an increased maximum reserve amount of $5,000, while a person who is a member of a couple and/or has a dependent child will now have an increased maximum reserve amount of $10,000.

The change will affect applicants for Newstart Allowance, Youth Allowance, Sickness Allowance and Austudy payments.

For more information:

- **Speak to your financial adviser**

Disclaimer