

Federal Budget Update 2010

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Highlights of the 2010 Budget

- **Key points on Super**
 1. **Permanent reduction to Government Co-contribution**
 2. **Minimum pension reduction NOT extended**
 3. **Super changes announced in response to Henry Report**

- **Key points on Taxation**
 1. **Reductions in Personal Income Tax**
 2. **Reductions in Personal Income Tax – Senior Australians**
 3. **Increase in the Medicare levy low income thresholds**
 4. **Standard tax deductions**
 5. **50% discount on up to \$1,000 interest income**
 6. **Increase in the net medical expense tax offset claim threshold**
 7. **Senior Australians Tax Offset**

Overview

As Treasurer Swan and PM Rudd have been constantly stating over the past week, the Federal Budget handed down tonight had, from a financial services perspective, few surprises and few new measures announced.

For a pre-election Budget you could even call it “no-frills” or austere with Swan stating that all new spending measures were to be offset by new savings measures and that spending was capped at 2% growth. The Government certainly wants to be seen as responsible economic managers going into the next election.

Unsurprisingly, the Government re-affirmed the changes announced a week ago in their “A Tax Plan for our Future” (or their response to the Henry Report).

There were few new super measures (other than those announced last week) with last year’s reduction in the co-contribution made permanent and some minor amendments to clarify current legislation.

A new savings measure to reduce income tax payable on interest bearing accounts was announced to encourage personal savings. This measure specifically targets lower income earners and older Australians.

We have outlined those measures that have most impact on your savings, investment and taxation situation. If you have any questions regarding how these changes will impact your personal circumstances, you should speak to your financial planner.

Details – Superannuation

1. Permanent reduction to Government Co-contribution

Effective date: 1 July 2010

The current maximum Government co-contribution of \$1,000 and the 100% matching rate will be permanently retained. In addition, indexation of the lower co-contribution threshold will be frozen for two years meaning the threshold will remain at the current level of \$31,920 for 2010/11 and 2011/12.

In last year's budget, the Government announced the temporary reduction to the maximum co-contribution and matching rate with plans to apply gradual increases to return the maximum co-contribution to \$1,500 and the matching rate to 150% by 2014/15. This will no longer occur.

The following table shows how the co-contribution entitlement for different income ranges:

Total Income	Co-contribution Entitlement
\$31,920 or less	\$1,000
\$31,920 - \$61,920	\$1,000 less 3.333 cents for each \$1 of total income over \$31,920
\$61,920	No entitlement

Impact

As a rule of thumb, for 2010/11, individuals with total income under \$54,500 pa and \$1,000 of after tax money available to contribute to super will be better off making an after-tax contribution of \$1,000 than salary sacrificing an equivalent pre-tax (grossed up) amount. This is because the benefit received by the Government co-contribution is higher than the equivalent tax savings available through salary sacrifice.

2. Minimum pension reduction NOT extended

The Government has NOT extended the 50% reduction in minimum annual payment amounts for certain retirement income streams. The standard minimum pension payments will apply from the 2010/11 financial year onwards.

Impact

Centrelink/DVA clients who were receiving less than the standard minimum payment in 2009/10 should be aware that their Centrelink benefits may be affected. These clients will need to advise Centrelink/DVA of their change in circumstances within 14 days. This is an existing Centrelink/DVA requirement for notification of change in circumstances.

3. Increasing the Superannuation Guarantee rate to 12%

The Superannuation Guarantee (SG) rate will be increased from 9% to 12% by 1 July 2019. This will commence with a 0.25% increase for the 2013/14 financial year. The table below illustrates the proposed time table for the full 3% increase.

Start date 1 July 2013

Financial Year	SG Rate (%)
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

Impact

In the long term, employees will have more savings in retirement, placing less pressure on the Age Pension. The decision to defer the commencement of the rate increase until 2013/14 recognises that employers and employees will need time to factor these increases into their future wage negotiations.

4. **SG age limit increase from 70 to 75** The Superannuation Guarantee (SG) age limit will be raised from 70 to 75. Currently, compulsory SG only applies to those aged less than 70.

This proposed change is due to commence on 1 July 2013.

Impact

- The increase to age 75 aligns the SG age limit with the age limit for personal and voluntary employer contributions, simplifying superannuation contribution requirements.
- Provides greater incentive for mature workers to remain in the workforce.
- The deferred start date allows employers and employees time to factor these increases into their future wage negotiations.

5. **Low income earners Government contribution**

The Government plans to introduce a Government superannuation contribution for low income earners. Individuals will need to have an adjusted taxable income (ATI) of less than \$37,000 to receive up to a maximum of \$500 per year.

The Government contribution would be calculated as 15% of the concessional contributions paid by or for individuals with an ATI less than \$37,000.

The maximum contribution of \$500 is equivalent to the tax an employee with an ATI of \$37,000 would pay on their SG contributions calculated as follows.

$$\$37,000 \times 9\% \text{ (SG rate)} = \$3,330 \times 15\% \text{ (tax rate deducted by super fund)} = \$499.50.$$

Note that by 1 July 2012, when this measure is proposed to commence, the marginal rate of tax for individuals earning between \$6,001 and \$37,000 will be 15% (this income tax threshold change is already legislated to apply from 1 July 2010).

The first Government contributions are expected to be paid into an eligible individual's superannuation account during 2013/14 for concessional contributions made during 2012/13. This payment lag is similar to the existing Government Co-contribution arrangements.

Individuals may be eligible for both the "low income earners Government contribution" and the existing Government Co-contribution.

Impact

This measure effectively means for eligible individuals the 15% tax on concessional contributions will be refunded making super an attractive savings vehicle for all taxpayers; not just those on a marginal tax rate greater than the super fund tax rate.

It is unclear whether this measure is limited to SG or all concessional contributions.

6. **Changes to the Concessional Contributions cap**

Currently the transitional concessional contributions cap is \$50,000 per annum for those aged 50 and older. This transitional cap will expire on 30 June 2012. It will, however, now be replaced with a new concessional contributions cap from 1 July 2012 for individuals aged 50 or over who "need" to make catch-up contributions. Under the new concessional contributions cap, individuals will be able to make (or have made on their behalf) concessional contributions of \$50,000 pa provided they are:

- aged 50 and over; and
- have total superannuation balances of less than \$500,000.

Impact

While the new concessional contributions cap for those aged 50 and over is not as generous as the current one, it is better than not having one at all. It will provide benefits to many:

- undertaking transition to retirement strategies;
- who delay focusing on building up their retirement assets until they have paid off their mortgage and educated their children; and
- who may have made unwise investment decisions, or experienced a down turn in investment markets.

Clients who reach age 50, but who have total superannuation of over \$500,000 will not benefit from this change.

7. No change to non-concessional contributions cap

The Government has reaffirmed the existing level of the non-concessional caps. Eligible individuals under the age of 75 will still be able to make non-concessional contributions to superannuation up to \$150,000 per year. Those who are under 65 can also bring forward two years' worth of non-concessional contributions, allowing them to contribute up to \$450,000 of non-concessional contributions in any three-year period.

Impact

No change.

Details – Taxation

1. Reductions in Personal Income Tax

Effective date: 1 July 2010

These reductions in personal income tax have been previously legislated by the Rudd government. The changes include an increase in the amount of income you can earn before moving into the 30% tax bracket. In addition the 38% tax rate is decreasing to 37%.

These new tax rates are shown against the current rates below:

Tax Thresholds 1 July 2009		
Low Threshold	High Threshold	Tax Rate %
-	6,000	-
6,001	35,000	15
35,001	80,000	30
80,001	180,000	38
180,001		45
Tax Thresholds 1 July 2010		
Low Threshold	High Threshold	Tax Rate %
-	6,000	-
6,001	37,000	15
37,001	80,000	30
80,001	180,000	37
180,001		45

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

The below table shows the tax savings for the 2010/11 financial year as compared to the 2009/10 financial year for a range of taxable incomes.

Reduced Tax Payable in 2010/11	
Income (\$)	Tax Savings (\$)
20,000 – 35,000	150
40,000 – 60,000	450
65,000	400
70,000 – 80,000	300
85,000	350
90,000	400
100,000	500
110,000	600
120,000	700
130,000	800
140,000	900
150,000	1,000
160,000	1,100
170,000	1,200
180,000+	1,300

The Low Income Tax Offset will increase from \$1,350 to \$1,500 for 2010/11, phasing out after \$30,000 by 4 cents in the dollar until phasing out completely until taxable income reaches \$67,500.

Impact

From 1 July 2010:

- All income earners with taxable income of more than \$15,000 will receive a higher net income as a result of either the increase in the Low Income Tax Offset and/or the increase in the 30% tax bracket.
- Individuals will not be subject to tax until their taxable income exceeds \$16,000 (up from \$15,000). This means those with taxable income up to \$30,000 will receive the first \$16,000 tax free.

- Salary sacrificing these tax savings to superannuation on a before-tax basis is a tax effective way to increase a client's superannuation balance, without affecting current after-tax income. Existing and new salary sacrifice arrangements should be reviewed to ensure that the concessional contributions cap is not exceeded (for 2010/11 this is \$25,000 or \$50,000 for individuals aged 50 or over).

For investors on lower marginal tax rates, using these tax savings to make personal after-tax contributions together with the Government co-contribution will generally give a better result.

2. Reductions in Personal Income Tax – Senior Australians

The reductions in personal income tax result in an increase in the amount of income that a Senior Australian Tax Offset (SATO) recipient can receive without paying tax. The Medicare Levy threshold that applies to Senior Australians will also increase to ensure that SATO recipients do not pay the Medicare Levy until they begin to incur an income tax liability.

From 1 July 2010:

	2009/10	2010/11	Extra Tax Free Income
Single	\$29,867	\$30,684	\$817
Couple	\$51,360	\$53,360	\$2,000

Impact

In addition to receiving tax free income from retirement income streams, individuals aged 60 and over will be able to receive higher levels of income outside super before being subject to tax.

3. Increase in the Medicare levy low income thresholds

Effective date: 1 July 2009

The Government has announced new Medicare levy thresholds that are applicable for the current financial year (ending 30 June 2010). These are \$18,488 for individuals (previously \$17,794) and \$31,196 for families (previously \$30,025). The increase on these thresholds for each dependent child or student will be \$2,865.

The low income threshold for pensioners below age pension age has been increased to \$27,697 for the year ending 30 June 2010. This will ensure such pensioners do not pay the Medicare levy when they do not have an income tax liability.

4. Standard tax deductions

Effective date: 1 July 2012 for standard \$500 deduction 1 July 2013 for standard \$1,000 deduction

Individual taxpayers will have the option of receiving a standard deduction for work related expenses and the cost of managing tax affairs. Taxpayers with deductible expenses greater than the standard deduction amount will be able to claim their higher expenses when lodging their tax return under the existing rules. The standard deduction will be \$500 in 2012/13 and will increase to \$1,000 from 1 July 2013.

Impact

- Taxpayers will spend less time and effort in preparing 'simpler' tax returns or as the Treasurer says "less time with the TaxPack and more time with the loved ones".
- The Government recognises this as being an important step towards a 'tick and flick' system of pre-filled tax returns.
- The Government estimates that 4.6 million individuals will be financially better off with the standard \$500 deduction in 2012/13. From 1 July 2013, an estimated 6.4 million individuals will benefit from the increased \$1,000 standard deduction.

5. 50% discount on up to \$1,000 interest income

Effective date: 1 July 2011

The Government has announced a 50% discount on the first \$1,000 of interest income.

From 1 July 2011, the Government will provide individuals a 50% tax discount on up to \$1,000 of interest earned from a range of savings products. The savings products attracting the concessions include bonds,

debentures and annuity products as well as deposits held with a bank, building society or credit union.

Example A: On 1 July, 2011 an individual deposited \$10,000 in a one-year term deposit with an effective rate of 5% per annum, earning \$500 after one year. The tax payer would be required to include only \$250 of this interest income in their tax return.

Example B: On 1 July, 2011 an individual deposited \$40,000 in a one-year term deposit with an effective rate of 5% per annum, earning \$2,000 after one year. The tax payer would be required to include only \$1,500 of this interest income in their tax return.

The Government plans to consult on the details of the operation of this concession including on how it would apply to interest earned indirectly by individuals, such as through a trust or managed investment scheme.

The Government has announced this measure in recognition of the fact that most interest income is taxed at the individual's marginal rate, while capital gains, made on assets held longer than 12 months, receive a 50% discount.

Impact

- The tax concession will most likely benefit older Australians or individuals with small amounts to invest.
- Below we have compared leaving \$10,000 in a bank account, with making a \$10,000 after-tax contribution to superannuation. The results are shown over a 5 and 10 year period.

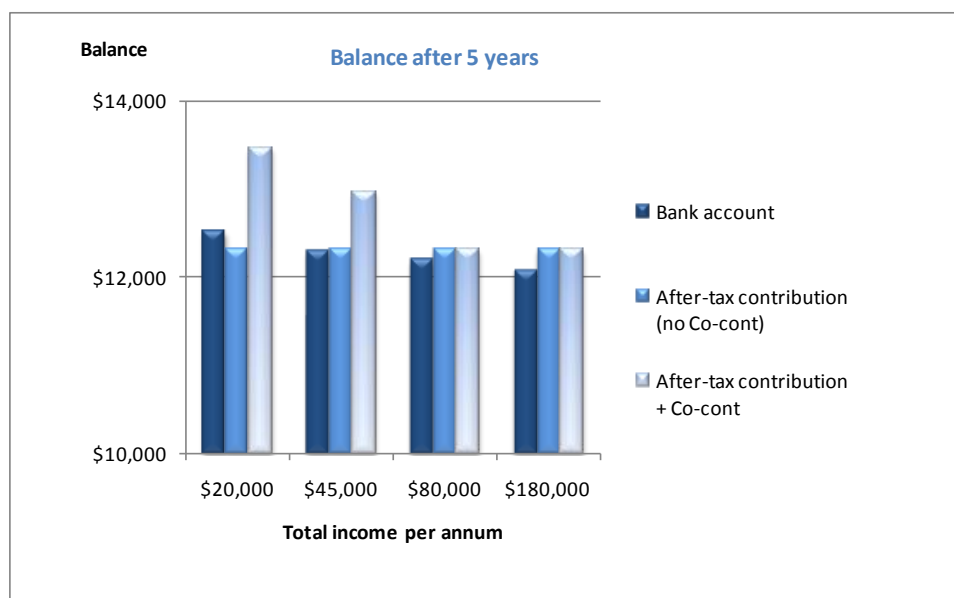


Figure 1 Balance after five years

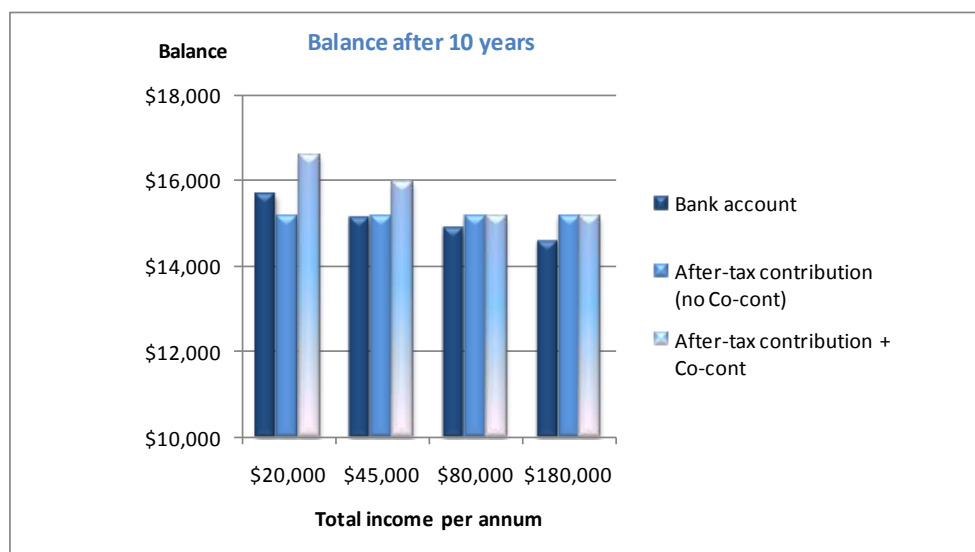


Figure 2 –balance after ten years

Assumptions:

- One \$10,000 investment made on 1 July 2011
- Effective income return of 5% per annum (no growth return) inside and outside super
- Where applicable the co-contribution is received in the 2012/2013 financial year based on the contribution made on 1 July 2011
- The 50% discount applies on the first \$1,000 of interest income received from the bank account
- Tax payable on the interest income is deducted from the bank account
- Interest income within the superannuation fund is taxed at 15%
- Individual is eligible to contribute to superannuation and has not exceeded their non-concessional contributions cap
- Co-contributions starts to phase out once an individual's total income exceeds \$31,920 and completely phases out once their income reaches \$61,920

Conclusions:

- Younger individuals will need to consider preservation issues when deciding between superannuation and interest accounts.
- Where preservation is less of a concern, then superannuation may be the preferred investment vehicle, especially where the individual is eligible for the Government Co-contribution or on a high marginal tax rate.
- Low income earners who are not receiving 10% or more of their income from employment or eligible business activities (or both) are not eligible for the Government Co-contribution.
- It is important to remember that while it may be possible for an individual to contribute to superannuation until age 75 if gainfully employed, only those aged 70 or younger at the end of the income year are eligible for the Government Co-contribution.

6. Increase in the net medical expense tax offset claim threshold

Effective date: 1 July 2010

The Government has announced an increase in the threshold above which a taxpayer may claim the 20% net medical expense tax offset from \$1,500 to \$2,000.

To date the threshold has not been indexed, however going forward the threshold will be indexed annually to the Consumer Price Index.

Disclaimer

The information contained in this document dated 11 May 2010 has been given in good faith and has been derived from laws current at this date and our interpretation of them. It has also been devised from the 2010 Federal Budget Papers, Ministerial statements, associated materials, and our interpretation of them. The taxation position described is a general statement and should only be used as a guide. It does not constitute tax advice. This document is to be used as general information only and should not be considered a comprehensive statement on any matter and should not be relied upon as such. This document has been prepared without taking into account any individual objectives, financial situation or needs. No member of the Westpac Group, or the BT Financial Group, nor any of their employees or directors gives any warranty of accuracy or reliability nor accepts any liability in any other way, including by reason of negligence for any errors or omissions contained herein, to the extent permitted by law. This document may not be used or reproduced without the prior consent of the BT Financial Group.