

Issued May 2010

On 2 May 2010 the Henry Review on Australia's Future Tax System ("AFTS") was released along with the Government's response. The Government's response proposed the introduction of a new resource super profits tax (RSPT), a reduction in company tax, an increase in small business concessions and significant changes to superannuation. The proposals are the first step in a tax reform agenda which may continue for the next decade.

The Henry Review has made a total of 138 recommendations. Besides the recommendations that have been accepted, a number have been specifically rejected. There are some areas which have been flagged for future reform and were not discussed in detail as part of the Government's response.

Company tax rate to be cut

The company tax rate is proposed to reduce from the current level of 30% to 29% for the 2013-14 financial year and to 28% for the 2014-15 financial year.

This will fall in line with international models and aims to encourage incentives to invest and greater distribution of income within the economy.

Eligible small business will get a head start with access to the reduction in the company tax rate by reducing the rate to 28% in the 2013-14 financial year for eligible small business companies. This will increase cash flow for these businesses and enable them to reinvest more back into the company for business expansion. Consultation with industry will occur prior to the introduction of the legislation.

It may be worthwhile to consider bringing forward expenses and delaying receipt of income to the lower tax years.

Small business asset write off

From the 2012-13 financial year the existing capital allowance of \$1,000 which is available to small business is proposed to be increased to \$5,000. In addition, the small business write-off provisions will be consolidated in a single asset pool rather than the two different depreciation pools that apply under the current rules.

The aim of this is to simplify the operation of the rules and to increase the cash flow of a small business, reduce compliance costs and make ownership of assets by the business more attractive than leasing or debt financing.

It may be worthwhile to consider delaying purchasing items to take advantage of the changed arrangements.

Increased Super Guarantee rate

The Government has announced that it plans to increase the Superannuation Guarantee (SG) rate from 9 to 12 per cent over time. The rate will be increased from 1 July 2013 to 1 July 2019 with increments of 0.25 percentage points in the first two years and 0.5 percentage points thereafter.

Year	Rate (%)	Increase (%)
2013/14	9.25	0.25
2014/15	9.50	0.25
2015/16	10.00	0.50
2016/17	10.50	0.50
2017/18	11.00	0.50
2018/19	11.50	0.50
2019/20	12.00	0.50

Super Guarantee age limit increased to 75

The Government has announced that it plans to increase the Superannuation Guarantee (SG) age limit from 70 to 75 from 1 July 2013.

It is intended that increasing the SG age limit will provide an incentive for mature workers to remain in the workforce.

Around 33,000 employees are expected to benefit from this measure.

Retaining of higher concessional contribution cap for those 50 or over

The \$50,000 concessional contribution cap for those aged 50 or over is proposed to be permanently adopted. There is, however, an additional condition. In order to qualify for the higher cap (the lower cap being \$25,000), an individual would have to have less than \$500,000 in super.

The "transitional" cap for those 50 or over is due to end on 1 July 2012. This would have meant that all individuals would have had the same concessional cap of \$25,000 (or its indexed equivalent). The new measure means the higher cap will remain in place beyond that date. This will enable individuals to make higher pre-tax contributions later in their lives when they are more likely to have the ability to do so.

Government Superannuation Contribution for low income earners

From 1 July 2012, a new superannuation contribution of up to \$500 (non-indexed) is proposed to be provided for workers with adjusted taxable income of up to \$37,000.

This will provide a taxation concession on superannuation guarantee contributions to individuals who have a 15% marginal tax rate.

How does the measure work?

The amount is calculated by applying a 15% matching rate to concessional contributions for individuals with adjusted taxable income of up to \$37,000.

To receive the maximum annual payment of \$500 an individual is required to receive superannuation guarantee contributions of \$3,333.

The Government contribution is expected to be paid to qualifying individuals in 2013/14 and will be paid directly into the individuals super fund.

Case study:

Joe is an employee of XYZ Pty Ltd. He is on a wage of \$28,000 which attracts superannuation guarantee contributions of \$2,520 (9% x \$28,000). Tax of \$378 (15% x \$2,520) is levied on superannuation guarantee contributions.

As Joe's income is below the threshold of \$37,000, the Government will make a contribution of \$378 to his superannuation fund. This effectively results in no tax being paid on his superannuation guarantee contributions.

Personal income tax returns

The Government is considering further changes to personal income tax returns to result in a simpler system with lower compliance costs. The announcements on reducing the burden the tax system places on individuals will be made in the coming months.

The Henry review's recommendations

Whilst the Government has accepted a handful of the Henry Tax Review's 138 recommendations and is understood to be considering many others, it has also rejected a number.

The recommendations most relevant to financial planning, and some Government reaction to them, are outlined below.

Investment tax discounts

A 40 per cent savings income discount to individuals for non-business related:

1. net interest income;
2. net residential rental income (including related interest expenses);
3. capital gains (and losses); and
4. interest expenses related to listed shares held by individuals as non-business investments.

Capital gains tax

The capital gains tax regime should be simplified by:

1. increasing the exemption threshold for collectables and exempting all personal use assets;
2. rationalising and streamlining the current small business capital gains tax concessions by:
 - removing the active asset 50 per cent reduction and 15-year exemption concessions;
 - increasing the lifetime limit of the retirement exemption by permanently aligning it with the capital gains tax cap for contributions to a superannuation fund; and
 - allowing taxpayers who sell a share in a company or an interest in a trust to access the concessions via the turnover test.
3. removing current grandfathering provisions relating to assets acquired before the commencement of capital gains tax, with a market value cost base provided for those assets when the exemption is removed, or before the end of previous indexation arrangements. A relatively long lead-time should be provided before these removals take effect; and

- rewriting the capital gains tax legislation using a principles-based approach that better integrates it with the rest of the income tax system.

The Government has ruled out reducing the CGT discount, applying a discount to negative gearing deductions or changing the grandfathering arrangements for CGT.

Superannuation

The Government confirmed it did not intend to remove tax free superannuation payments for those aged 60 or older.

Changes to contributions tax

The tax on superannuation contributions in the fund should be abolished. Employer superannuation contributions should be treated as income in the hands of the individual, taxed at marginal personal income tax rates and receive a flat-rate refundable tax offset.

- An offset should be provided for all superannuation contributions up to an annual cap of \$25,000 (indexed). The offset should be set so the majority of taxpayers effectively do not pay more than 15 per cent tax on their contributions. The cap should be doubled for people aged 50 or older.
- An annual cap on total contributions should continue to apply.
- The offset should replace the superannuation cocontribution and superannuation spouse contribution tax offset.
- Compulsory superannuation contributions made by employers should not reduce eligibility for income support or family assistance payments. They should also not form part of the calculation for child support.

Reduction of tax on earnings

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

Contributions and preservation

The restriction on people aged 75 and over from making contributions should be removed. However, a work test should still apply for people aged 65 and over. There should be no restrictions on people wanting to purchase longevity insurance products from a prudentially regulated entity.

An increase in the preservation age should apply to people who currently have a legislatively prescribed retirement age. The Government has, however, ruled out this recommendation.

Superannuation guarantee

Superannuation guarantee contributions should be paid at the same time as wages. This should be introduced over time so businesses can adjust their cash flows. As a first step, larger businesses (that is, businesses required to lodge their business activity statements on a monthly basis) should be required to pay superannuation guarantee contributions at least monthly.

Employers should report superannuation contributions to their employees when a contribution is made.

There should be a method of linking superannuation records, such as client identifiers like the tax file number, to make it easier for people to manage their superannuation.

A superannuation portal where people can interact with government agencies and get information on retirement incomes should be developed. Over time this portal should evolve, subject to suitable safeguards, so that people can manage all their superannuation through one channel.

Government

The government should support the development of a longevity insurance market within the private sector.

- The government should issue long-term securities, but only where this is consistent with its fiscal obligations, to help product providers manage the investment risk associated with longevity insurance.
- The government should make available the data needed to create and maintain a longevity index that would assist product providers to hedge longevity risk.
- The government should remove the prescriptive rules in the Superannuation Industry (Supervision) Regulations 1994 relating to income streams that restrict product innovation. This should be done in conjunction with the recommendation to have a uniform tax on earnings on all superannuation assets.

The government should consider offering an immediate annuity and deferred annuity product that would allow a person to purchase a lifetime income. The Government has ruled out offering a Government annuity product.

Social security

Overall structure

There should be three categories of income support payments:

1. A **pension category** for people who are not expected to support themselves through paid work, including the aged, disabled or carers. This pension would be paid at a rate that provides a basic acceptable standard of living, having regard to prevailing community standards.
2. A **participation category** for people of working age who are expected to support themselves through paid work now or in the near future. This would cover the unemployed including youth (both under and over 18), those who are temporarily incapacitated, people with a partial capacity to work and primary carers of dependent children. This would be paid at a rate that is less than the pension rate. Parents on income support would receive a higher total level of payment. Unemployed youth aged less than 21 would be paid no more than full-time students to avoid creating incentives to leave full-time study for unemployment.
3. A **student assistance category** for people engaged in full-time study. Students aged 21 and over would continue to be paid at a lower rate than the unemployed and at the same rate as younger students in similar circumstances. Students could be given the ability to borrow against future income to supplement their student assistance.

Means testing

The current income and asset tests for income support payments should be replaced. The new tests should:

1. extend deemed income on assets in addition to financial assets, including superannuation income streams, rental housing and other asset classes (whether income-producing or not). Superannuation income streams where deeming income would be difficult to apply would be tested on gross income but with a fair deduction for capital;
2. have low and high deeming rates based on the returns expected from a portfolio of assets held by a prudent investor. These rates should be set by reference to an appropriate benchmark;
3. continue the means test exemption for owneroccupied housing up to a high indexed threshold;
4. set a high capped exemption for personal-use assets;
5. retain the current concessional treatment of employment income for certain allowances and pensions;
6. have different free areas for pensions and allowances; and
7. remove the liquid assets waiting period and the sudden-death cut-out that applies to people on certain payments.

The Government has ruled out any change to the means testing of the family home.

Family assistance

Means testing for family assistance payments should be based on the same measure of taxable income as for income tax, including fringe benefits. However, payment should not be reduced as a result of the inclusion of compulsory superannuation contributions in taxable income.

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