

BUDGET OVERVIEW

(1) INTRODUCTION

At 7.30pm on 8 May 2007, the Treasurer, Peter Costello, delivered the 2007-08 Commonwealth Budget. The Treasurer is forecasting a cash surplus for the 2007-08 year of \$10.6 billion, with the fiscal or accrual surplus estimated at \$10 billion. On top of the income tax cuts announced last year, there are further income tax cuts, to take effect in two stages, from 1 July 2007 and 1 July 2008.

The Treasurer said that the 2007-08 Budget tax cuts ensure that over 80% of taxpayers face a top marginal tax rate of 30% or less. A taxpayer will need to earn \$134,000 to pay an average tax rate of 30% in 2008-09. Taxpayers will not reach the top marginal tax rate until they earn more than three and a half times average weekly earnings in 2008-09.

Other changes include a package of measures that will make it easier for small businesses to meet their tax obligations. Included in the package is a proposal to give more small businesses the option of using a simplified method to calculate their GST. From 1 July 2007, any small business that makes mixed (taxable and GST free) supplies or mixed purchases will be able to approach the ATO to discuss the development of a simplified accounting method for their use.

Large business will also be pleased to see that the \$100 million cap on the application of the same business test has been removed retrospectively with effect from 1 July 2005.

A summary of the Budget details are set out below.

(2) IS EVERYONE A WINNER IN THE 2007-08 BUDGET?

There is no doubt that many low and middle income Australian taxpayers are winners under the 2007-08 Budget. It is also clear that there are substantial wins for business in general, including small business.

However, the Government has only been selective about reducing the complexity of our tax laws in this Budget. In going forward, we continue to encourage the Government to work towards simplifying the tax system and a good place to start is by removing the

complexities that exist due to the wide gap between the corporate tax rate and the highest marginal tax rate for individuals.

JARGON

ATO	Australian Taxation Office
BAS	Business Activity Statement
CCB	Child Care Benefit
CGT	Capital Gains Tax
CCTR	Child Care Tax Rebate
COT	Continuity Of Ownership Test
HEEF	Higher Education Endowment Fund
PAYG	Pay As You Go
SATO	Senior Australian Tax Offset
SBT	Same Business Test
SNI	Separate Net Income
SMSF	Small Managed Superannuation Fund

PERSONAL INCOME TAX

(4) MAKING IT EASIER TO COMPLETE TAX RETURNS

The Government will provide additional funding of \$20 million in 2007-08 to enable the ATO to pre-fill electronic individual income tax returns for the 2007-08 and following income years.

The pre-filling of tax returns will make completing income tax returns easier for around nine million individual taxpayers who use e tax or lodge their returns through tax agents. These taxpayers account for around 80% of all individual taxpayers. Nearly one million taxpayers will need to do no more than lodge their pre filled return electronically. Millions more will need to provide only a few additional pieces of information to complete their returns.

The ATO will automatically include the following information in returns:

- salary, wages and allowances, where the employer has electronically lodged the employee's payment summary with the ATO;
- dividend and interest income and distributions from managed funds;
- payments from Centrelink, the Department of Education, Science and Training and the Department of Veterans' Affairs;
- Medicare out of pocket expenses and private health insurance information; and
- Higher Education Contribution Scheme and Higher Education Loan Programme details.

The ATO will progressively pre fill this information as it is received. Most information is expected to be received by mid August.



This information will also be available to tax agents to help them complete returns on behalf of their clients. .

(5) LOW INCOME OFFSET

From 1 July 2007, the low income tax offset will increase from \$600 to \$750 per year. In addition, the income threshold at which the offset begins to reduce will increase from \$25,000 to \$30,000. As a result, some offset can be claimed up to an income of \$48,750 compared to \$40,000 currently. Those eligible for the full income tax offset will not pay tax until their annual income exceeds \$11,000 (up from \$10,000 currently).

(6) SENIOR AUSTRALIANS

Senior Australians eligible for the senior Australians tax offset currently pay no tax up to an annual income of \$24,867 for singles and \$41,360 for couples (depending on the income earned by each member of the couple). The effect of the tax cuts is to lift these income levels up to \$25,867 for singles and \$43,360 for couples.

The Medicare levy threshold that applies to senior Australians will be increased to ensure that senior Australians do not pay the Medicare levy until they begin to incur an income tax liability.

(7) INCREASE IN DEPENDENT SPOUSE REBATE

The Government will increase the dependent spouse rebate from \$1,655 to \$2,100 with effect from 1 July 2007. This measure will increase the separate net income at which the rebate is completely phased out from \$6,901 to \$8,681.

(8) INCREASE IN MEDICARE LEVY LOW-INCOME THRESHOLDS

The Government will increase the Medicare low income thresholds to \$16,740 for individuals and \$28,247 for families, with effect from 1 July 2006. The additional amount of threshold for each dependent child or student will also be increased to \$2,594. The increase in these thresholds takes into account movements in the Consumer Price Index and ensures that low income families and individuals are exempt from paying the levy.

The Medicare levy low income threshold for pensioners below age pension age will also be increased. From 1 July 2006, the threshold will rise to \$21,637. This will ensure that pensioners below age pension age do

not pay the Medicare levy while they do not have an income tax liability.

(9) PERSONAL INCOME TAX CUTS

The Government will provide tax cuts worth \$31.5 billion over the next 4 years. This is in addition to the \$36.7 billion worth of tax cuts announced in last year's budget.

From 1 July 2007, the 30% threshold will rise from \$25,001 to \$30,001.

From 1 July 2008, the 40% threshold will rise from \$75,001 to \$80,001 and the 45% threshold will rise from \$150,001 to \$180,001.

Current	Rate
Income range	%
\$0 – \$ 6,000	0
\$6001 – \$25,000	15
\$25,001 – \$75,000	30
\$75,001 – \$150,000	40
\$150,000 +	45
From 1 July 2007	Rate
Income range	%
\$0 – \$6,000	0
\$6,001 – \$30,000	15
\$30,001 – \$75,000	30
\$75,001 – \$150,000	40
\$150,000 +	45
From 1 July 2008	Rate
Income range	%
\$0 – \$6,000	0
\$6,001 – \$30,000	15
\$30,001 – \$80,000	30
\$80,000 – \$180,000	40
\$180,000 +	45

CAPITAL GAINS TAX

(10) EXTENDING SMSF ROLL OVER ON MARRIAGE BREAKDOWN

The Government will allow one spouse in a marriage breakdown to transfer their entire in specie interest in a small superannuation fund to another complying superannuation fund, without there being an immediate capital gains tax (CGT) taxing point. This measure will have effect from 1 July 2007.

Currently, the CGT roll over for assets of small superannuation funds on marriage

breakdown applies only to the spouse who benefits from a payment split made under the Family Law Act 1975 and only to the assets subject to the payment split. These assets can be rolled over only to another small superannuation fund.

The amendment recognises that it is often in the interests of spouses in a marriage breakdown not to continue to provide for their future superannuation arrangements through a single small superannuation fund. The amendment will also provide greater choice of fund to the spouse whose interest is transferred.

CORPORATE TAX

(11) SAME BUSINESS TEST AND TECHNICAL AMENDMENTS

The Government will remove the \$100 million cap on the same business test (SBT), with effect from 1 July 2005.

Currently, a company is able to carry forward a tax loss to offset future assessable income, subject to meeting the continuity of ownership test (COT), or if the COT is not satisfied, the SBT applies. Companies with income in excess of \$100 million do not have access to the SBT.

The removal of the SBT cap will assist large closely held companies that do not benefit from the relaxation of the COT. The other amendments to the loss recoupment rules will reduce uncertainty and ensure that the outcomes under the rules are consistent with policy intent.

(12) FURTHER CONSOLIDATION AMENDMENTS

The Government will improve and clarify the operation of the income tax law for consolidated groups. The measure will generally take effect from 1 July 2002, the commencement of the consolidation regime, though some aspects have more recent dates of commencement.

The measure includes changes to the consolidation tax cost setting rules, the capital gains tax provisions and the uniform capital allowances rules. The measure will ensure that the income tax law affecting consolidated groups operates as intended and will reduce the compliance burden for consolidated groups.

(13) CONSOLIDATION AND ADIs

The Government will remove taxation

impediments to the restructuring of conglomerates containing authorised deposit taking institutions (ADIs) involving the appointment of a non operating holding company as the head company of the consolidated group, with effect from 1 July 2007.

Currently, if a consolidated group headed by an ADI were to restructure and appoint a non operating holding company as the head company of the group, the ADI would become a subsidiary company and would not be able to issue preference shares outside the group.

The measure will ensure that ADIs, as subsidiary members of a group, can continue to issue certain preference shares to non group members and maintain their tax position. The measure will also ensure that ordinary shareholders who dispose of their shares in an ADI, in exchange for shares in the non operating holding company, can obtain a capital gains tax roll over.

(14) FINANCE LEASING TAX RULES TO REMAIN UNCHANGED

The Government will not proceed with the Review of Business Taxation recommendation relating to the taxation of finance leasing. The Government had announced, following the Review of Business Taxation, its in principle agreement to proceed with this proposal subject to further review. Proceeding with this proposal would disrupt the finance leasing sector and have an adverse impact on business more broadly, particularly small business. This decision will mean that finance leases will be excluded from the scope of forthcoming legislation for the taxation of financial arrangements.

GST

(15) INCREASE IN THE GST REGISTRATION TURNOVER THRESHOLD

The annual turnover thresholds for registration for the GST will be raised to \$75,000 for businesses and to \$150,000 for non profit bodies, with effect from 1 July 2007.

As a result of this measure, businesses and non profit bodies with a turnover between the present threshold (\$50,000 or \$100,000) and the proposed threshold (\$75,000 or \$150,000) will no longer be required to register for GST. Those that voluntarily

register for GST will have the option of remitting GST annually, rather than quarterly or monthly.

Taxpayers choosing not to register for GST will be able to claim, against their business income, the GST inclusive cost of deductible business expenses, rather than the GST exclusive amount. They will not be able to claim fuel tax credits.

This measure is subject to the unanimous agreement of the States and Territories.

(16) INCREASE IN THE THRESHOLD FOR REQUIRING AN APPROVED TAX INVOICE FOR GST

Businesses will be allowed to claim input tax credits for purchases with a GST exclusive value of \$75 or less without the need for an approved tax invoice, with effect from 1 July 2007.

To claim an input tax credit, businesses currently have to obtain an approved tax invoice for all purchases with a GST exclusive value greater than \$50. For purchases with a GST exclusive value of \$50 or less, the documentation required for income tax purposes is sufficient to claim an input tax credit.

This measure will also carry over to the "no ABN withholding" arrangements, increasing the threshold for "no ABN withholding" from \$50 to \$75.

(17) PAYG INSTALMENTS PAID ANNUALLY WHEN VOLUNTARILY REGISTERED FOR GST

The Government will align the pay as you go (PAYG) payment and reporting requirements with the annual payment and reporting requirements for taxpayers who are voluntarily registered for GST, with effect from 1 July 2008.

Currently, taxpayers can remit PAYG annually only if they are not registered for GST and they meet other eligibility requirements. This measure will allow taxpayers who voluntarily register for GST, and who report and pay GST on an annual basis, to meet their PAYG obligations on an annual basis, subject to the other eligibility tests.

The measure will reduce the compliance costs of eligible taxpayers, as they will be able to lodge only one Business Activity Statement per year.

(18) SIMPLIFIED ACCOUNTING METHODS - EXTENDING AVAILABILITY

The Commissioner of Taxation will have power to develop simplified accounting methods (SAMs) for all entities with an annual turnover of less than \$2 million that make mixed supplies - taxable and GST free - or mixed purchases, with effect from 1 July 2007.

Currently, SAMs are restricted to retailers that sell food and to charities that make GST free supplies. Under this measure, businesses will be able to approach the Australian Taxation Office to initiate the development of a SAM to simplify their GST calculations and reduce their compliance costs.

This measure is subject to the unanimous agreement of the States and Territories.

SUPERANNUATION

(19) ADDITIONAL GOVERNMENT CO-CONTRIBUTION

The Treasurer announced that the Government will pay a one off additional co contribution into the superannuation accounts of those persons who made eligible contributions in the 2005-06 income year. This payment will double the co contribution paid in respect of that year, and contribute an additional \$1.1 billion to the retirement savings of low to middle income earning Australians.

(20) PUBLIC OFFER FUNDS TO BE PREVENTED FROM IMPOSING A PARTICIPATING EMPLOYER REQUIREMENT

The Government will prevent public offer funds from requiring that new employers sign "participating employer" agreements before accepting contributions on behalf of fund members. The measure will have effect from 1 July 2007. Currently, funds may require employers to become a 'participating employer' in order to make contributions to an employee's existing fund.

This measure will generally allow employees to choose to remain in a fund following a change of employer, rather than having contributions paid to another fund.

OTHER MEASURES**(21) CHILD CARE TAX REBATE - CONVERSION TO A DIRECT PAYMENT**

The Government will convert the existing Child Care Tax Rebate (CCTR) to a direct payment administered through Centrelink at a cost of \$1.4 billion over five years (including \$451.0 million in 2006-07).

From 1 July 2007, families will receive the CCTR - which covers 30% of out of pocket costs, up to a maximum of \$4,000, plus indexation - as a direct payment, soon after the financial year in which they incur child care costs. The change means that the CCTR will be received nearer to the time when costs are incurred by parents compared to current arrangements.

Families will still receive a rebate for out of pocket costs incurred in 2005-06, under the existing tax system arrangements. This means families with out of pocket costs for both 2005-06 and 2006-07 will receive two rebates in 2007 08 - one through the tax system, and one as a direct payment.

The change in the delivery of the CCTR from a tax offset to a payment also means that families with insufficient tax liability to absorb their full CCTR entitlement will now receive their full rebate.

(22) ESTABLISHMENT COSTS FOR CARBON SINK FORESTS DEDUCTIBLE

The Government will introduce depreciation for the costs of establishing a qualifying carbon sink forest under the horticultural plant provisions, with effect from 1 July 2007. This will enable costs to be depreciated over a period of 14 years, which is considerably less than the effective life of such a forest.

As an additional enhancement to encourage the early establishment of carbon sink forests, the Government will introduce immediate deductibility for costs incurred in establishing a qualifying carbon sink forest during a five year period commencing on 1 July 2007. The immediate deduction will take precedence over the general horticultural provisions during this 5 year period. Deductions under this measure will not be available to carbon sink forests established through managed investment schemes.

Currently, the costs of establishing a carbon sink forest are regarded as capital in nature

and are treated under the CGT provisions of the tax law.

(23) AMOUNTS MISAPPROPRIATED BY AN AGENT - INCOME TAX TREATMENT

The Government will ensure a more consistent treatment of amounts misappropriated by an agent. This measure will have effect from the date of Royal Assent of the enabling legislation.

Currently, amounts misappropriated by an agent may reduce tax liabilities only in limited circumstances. There is no offsetting adjustment available where an amount misappropriated by an agent arises from the disposal of a depreciating asset or a capital gains tax asset.

This measure will extend the recognition of misappropriated amounts to calculations made under the uniform capital allowance and capital gains tax regimes.

(24) AUSTRALIAN PROPERTY TRUSTS - ENHANCING INTERNATIONAL COMPETITIVENESS

The Government will allow certain stapled entities, such as Australian listed property trusts, to restructure with an interposed head trust without taxation consequences, with effect from the 2006 07 income year.

Capital gains tax roll over relief will be provided for investors in a stapled group where a unit trust has been interposed between the investors in the stapled group and the stapled entities.

The Government will also ensure that these restructures do not result in the head trust being taxed as if it were a company.

(25) FORESTRY MANAGED INVESTMENT SCHEMES - TRADING OF INTERESTS

The Government will allow trading of both existing and future interests in forestry managed investment schemes (MISs), subject to a minimum four year holding period for initial investors, with effect from 1 July 2007.

Currently, it is possible to trade interests in forestry schemes only in exceptional circumstances. General trading has not occurred owing to a view that investors' contributions would not be deductible if there was evidence that the investor did not intend, at the time of entering the scheme, to carry on a business and remain in the scheme until harvest.

The measure will allow initial investors to trade their interests in a forestry MIS once they have been held for a period of at least four years. The four year restriction will apply only to the initial investors in a scheme. The trading of forestry MIS interests will be subject to a market value pricing rule for initial investors to reduce tax arbitrage opportunities. In addition, there will be specific rules for the income tax treatment of investors' costs and proceeds to ensure tax symmetry.

The measure will apply to interests in a pre existing forestry MIS as well as future investment in newly established schemes. This will mean that taxpayers who invested in a forestry MIS prior to 1 July 2003 will be able to trade their interest as of 1 July 2007.

(26) THIN CAP AMENDMENTS - EXCLUDED EQUITY INTEREST

The Government will change the definition of 'excluded equity interest' in the thin capitalisation rules to ensure that the rules operate as intended. This measure will apply to income years beginning on or after 1 July 2002.

To prevent manipulation of the thin capitalisation rules - through temporary, artificial inflation of equity and asset levels - certain short term equity interests are excluded from thin capitalisation calculations for income years beginning on or after 1 July 2002. This measure will ensure that taxpayers are not inadvertently disadvantaged by the exclusion of long term equity interests from thin capitalisation calculations.

(27) VENTURE CAPITAL IMPROVEMENTS

The Government will further relax the eligibility requirements for concessional taxation treatment for foreign residents investing in venture capital limited partnerships and Australian venture capital funds of funds, with effect from the 2007-08 income year.

The concessional tax treatment for foreign resident investors will be extended:

- to allow up to 20% of committed capital in venture capital limited partnerships and Australian venture capital funds of funds to be invested in companies and unit trusts that are not located in Australia; and
- to allow eligible partners in conditionally registered venture capital limited partnerships and Australian venture capital funds of funds that become fully registered to

be entitled to a tax exemption on the profits and gains derived from investments made while the partnership was conditionally registered.

To ensure that investments made by an early stage venture capital limited partnership are directed at early stage venture capital activities, a partnership can acquire pre-owned investments in an entity only if:

- it already owns an investment in the entity, or it will also be making investments, that are not pre owned investments in the entity at the same time; and
- the total value of the partnership's pre owned investments does not exceed 20% of its committed capital.

(28) DIVS 10BA AND 10B (FILM INCENTIVES) TO BE PHASED OUT

The Government has announced that the current investor tax incentives available through Division 10BA and Division 10B of ITAA 1936 will be phased out, with no new applications to be accepted after 30 June 2007. This will increase estimated taxation revenue by \$55.0 million over three years from 2008 09. The Film Licensed Investment Company scheme will not be renewed beyond its current expiry date of 30 June 2007.

In their place, a producer tax rebate will be introduced, by which Australian producers will be eligible for a 40% refundable rebate on feature films and a 20% refundable rebate on other media productions, including television series, documentaries, and mini series. To be eligible for the rebate, productions will be required to meet criteria, including creative control by Australians, and minimum qualifying expenditure thresholds depending on the type of production. The rebate will apply to expenditure incurred on eligible productions from 1 July 2007.

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