



12 May 2009

### 2009 Federal Budget Overview

No significant tax changes were announced in tonight's Budget, although measures have been proposed to reduce tax concessions for high income earners in the form of superannuation reform and changes to the private health insurance offset. Contrary to speculation, the incentive for first home owners has been extended and so has the small business tax break. Reform of the tax system is high on the agenda but tax cuts announced in last year's Budget will be honoured.

Here are the highlights of the tax and superannuation changes announced in the Budget.

### Superannuation concessions

#### Concessional contributions caps reduced

The government has made its first rollback of the simpler superannuation reforms, reducing the concessional contributions caps from the start of the 2009/10 income year. The concessional contributions cap has been halved to \$25,000 a year from its current limit of \$50,000. The government will introduce special concessions for persons who are defined benefit fund members on 12 May 2009.

A reduction will also apply to the transitional threshold for concessional contributions. The transitional concessional cap will be reduced from its current annual level of \$100,000 to \$50,000 per year. The transitional concessional cap of \$50,000 will apply for the 2009/10, 2010/11 and 2011/12 years of income.

The government has ruled out any reduction to the non-concessional caps at this time, stating that they remain at \$150,000 (indexed) which will now be six times the amount of the concessional cap for the 2009/10 income year and beyond.

#### Non-concessional Contribution Threshold

This remains at \$150,000 (scheduled to increase to \$165,000 at 1 July 2009). It will be indexed in line with the concessional contributions cap and will remain at six times that cap.

#### Minimum Pension Withdrawal Reduction

The account based minimum pension withdrawal requirements will continue to be halved for 2009/10. This is an extension of the initiative announced earlier this calendar year. This measure assists self-funded retirees by not forcing a sale of assets at reduced market values and allowing the capital base to be invested for the future.

#### Superannuation co-contribution decreased

The superannuation co-contribution scheme will be reduced to 100% of eligible contributions for 2009/10, 2010/11 and 2011/12 income years, with the rate

increasing to 125% of contributions for the 2012/13 and 2013/14 years and returning to its former level of 150% for the 2014/15 year.

The adjusted superannuation co-contribution rates from 1 July 2009 will be:

- 100% for 2009/10, 2010/11 and 2011/12, with a maximum co-contribution of \$1000, reduced by 3.333 cents for each dollar by which the person's total income exceeds the shade out threshold for receiving the full co-contribution;
- 125% for 2012/13 and 2013/14, with a maximum co-contribution of \$1,250, reduced by 4.167 cents for each dollar of total income above the shade out threshold; and
- 150% from 2014/15 onwards, with a maximum co-contribution of \$1,500, reduced by 5 cents for each dollar of total income above the shade out threshold.

### Individuals and families

#### Private Health Insurance Rebate

From 1 July 2010, the government will introduce three new "Private Health Insurance Tiers" in respect of the Private Health Insurance Rebate as follows.

- Tier 1: for singles earning more than \$75,001 (couples \$150,001), the Private Health Insurance Rebate will be 20% for those up to 65 years (25% for those over 65, and 30% for those over 70 years). The Surcharge for avoiding private health insurance will remain at 1%.
- Tier 2: for singles earning more than \$90,001 (couples \$180,001), the Private Health Insurance Rebate will be 10%, for those up to 65 years (15% for those over 65, and 20% for those over 70 years). The Surcharge for avoiding private health insurance will be increased to 1.25%.
- Tier 3: for singles earning more than \$120,001 (couples \$240,001), no Private Health Insurance Rebate will be provided. The Surcharge for avoiding private health insurance will be increased to 1.5%.

All income thresholds will continue to remain indexed.

For low and middle-income earners, the existing 30%, 35%, 40% Private Health Insurance rebates will remain in place.

#### Increase in Medicare levy low-income thresholds

From the 2008/09 year, the Medicare levy low-income thresholds will be increased to \$17,794 for individuals and \$30,025 for individuals in families. The additional amount of threshold for each dependent child or student will also increase to \$2,757.

Further, the government will increase the Medicare levy low-income threshold for pensioners below Age Pension age to \$25,299, with effect from 1 July 2008.

### First Home Owner's Boost extended

The First Home Owner's Boost (FHOB) will be extended for an extra six months and will be reduced by half for the last three months of the extension period.

For eligible first home buyers entering into contracts between 1 July 2009 and 30 September 2009 (inclusive) the FHOB will continue to provide \$7,000 for the purchase of established homes and \$14,000 for the purchase of new homes. This means that including the \$7,000 First Home Owner's Grant, until 30 September, purchasers of new homes will continue to be eligible for \$21,000 of assistance, and purchasers of existing homes will continue to be eligible for \$14,000 of assistance.

Between 1 October 2009 and 31 December 2009 the FHOB grants will be \$3,500 for the purchase of established homes and \$7,000 for the purchase of new homes. This means that including the \$7,000 First Home Owner's Grant, from 1 October until 31 December, purchasers of new homes will be eligible for \$14,000 of assistance, and purchasers of existing homes will be eligible for \$10,500 of assistance.

The FHOB grants are in addition to the existing \$7,000 grant under the First Home Owners Scheme.

### Family assistance - Paid Parental Leave scheme

The government has announced that it will introduce a Paid Parental Leave scheme for parents in respect of births and adoptions that occur on or after 1 January 2011. Parents will be able to lodge claims from 1 October 2010. The scheme will provide 18 weeks postnatal leave paid at the federal minimum wage (currently \$543.78 per week).

To be eligible for the scheme, a parent in paid work:

- must have worked continuously with one or more employers for at least 10 of the 13 months before the expected date of birth or adoption;
- must have worked at least 330 hours in those 10 months (equivalent to around one full day of work each week); and
- must have an adjusted taxable income of \$150,000 or less in the financial year prior to the date of birth or adoption of the child.

Parents who are eligible for Paid Parental Leave will be able to continue to access employer funded leave (maternity leave and recreation leave) around the time of the birth or adoption of a child.

Paid Parental Leave will be available to contractors, casual workers and the self-employed. Payments made under the scheme will be taxable. Parents who receive paid parental leave will not receive the Baby Bonus (except in the case of twins or multiple births), or FTB-B during the 18 week Paid Parental Leave period.

Mothers and primary carers not in full-time paid work will continue to receive the current forms of family assistance (including the Baby Bonus), if they meet the relevant eligibility requirements.

Superannuation payments will not initially be introduced for the Paid Parental Leave. Its introduction will be considered as part of a comprehensive review of scheme, within three years after the scheme's implementation.

### Family Tax Benefit and other family payments

From 1 July 2009, FTB-A payment rates will be indexed by the Consumer Price Index consistent with other family payments such as FTB-B and the Baby Bonus. This will replace the current arrangement whereby maximum rates of FTB-A for children under the age of 16 are benchmarked to a proportion of the combined couple rate of pension payments, or adjusted by the Consumer Price Index, whichever is higher.

The following higher income thresholds (which would ordinarily be indexed by the Consumer Price Index) for family payments will remain fixed until July 2012:

- the FTB-B primary earner income threshold, which will remain at \$150,000;
- the income threshold for receiving the dependency tax offsets, which will remain at \$150,000;
- the Baby Bonus eligibility threshold, which will remain at \$75,000 of family income in the six months following the birth or adoption of a child (equivalent to \$150,000 a year) and
- the higher income-free area of FTB-A, which will remain at \$94,316 of family income (plus \$3,796 for each child after the first).

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### Other Matters

#### Employee Share Schemes

Currently, under qualifying share schemes, an employee can elect to be assessed on discounts provided on shares or rights in the income year in which the shares or rights are acquired. If no election is made, the discount (which includes gains on shares or rights) is taxed at a later time (eg when the employee disposes of the share). If an employee elects to be taxed up front, they receive a tax exemption of up to \$1,000 on the discount. However, if the shares or options are issued under a non-qualifying share scheme, the employee is taxed on the discount when he or she acquires the shares or options.

Under the new arrangements, all discounts on shares and options under an employee share scheme, whether qualifying or non-qualifying, will be assessed in the year in which they are acquired. Therefore employees acquiring shares or options under qualifying share schemes will no longer be able to elect to defer taxation on their discount to a later time.

Further, the \$1,000 tax exemption will be limited to those employees with a taxable income of less than \$60,000 after adjustment for fringe benefits, salary sacrifice and negative gearing losses.

The measure will apply to shares and options acquired after 7.30pm on 12 May 2009.

### Non-commercial losses rules

From the 2009/10 income year, taxpayers with an adjusted taxable income of over \$250,000 will have excess deductions quarantined to the business activity under the non-commercial losses rules. The existing rules will continue to apply to taxpayers with an adjusted taxable income of \$250,000 or less. Taxpayers will still be able to apply for relief from the rules if there are exceptional circumstances or because the nature of the activities means that a taxpayer is temporarily carrying on an uncommercial business.

### Foreign employment income exemption changes

Currently, Australians working overseas for over 90 consecutive days are eligible for a general exemption which means they do not pay any Australian income tax on their foreign employment income.

From 1 July 2009, the foreign employment income exemption will only be available for income earned:

- as an aid or charitable worker employed by a recognised non-government organisation; or
- as a government aid worker; or
- as a specified government employee (for example, defence and police force personnel deployed overseas).

Income earned by an individual employed on an overseas project approved by the Minister for Trade as being in the national interest will remain exempt.

A tax offset will be available for any foreign tax paid on the foreign employment income.

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## Companies Small Businesses and Trusts

### Small Business Tax Break extended

The Small Business and General Business Tax Break will be expanded to allow a bonus deduction of 50 per cent to small businesses with a turnover of less than \$2 million that acquire an eligible asset between 13 December 2008 and 31 December 2009 and install it ready for use by 31 December 2010.

The previously announced 30 per cent and 10 per cent bonuses will continue to apply to all other businesses.

The budget announcement outlines an expansion of the "tax break" proposed for business taxpayers investing in eligible new depreciating assets or enhancing existing assets. Currently the Tax Laws Amendment (Small Business and General Business Tax Break) Bill 2009 provides for an additional deduction at a rate of 30% for investment committed by

30 June 2009, provided the asset is installed ready for use by 30 June 2010. The rate of deduction is proposed to fall to 10% for investment committed between 1 July 2009 and 31 December 2009 where installation of the asset is completed by 31 December 2010. This Bill is currently before parliament.

- It is assumed that the term "small businesses" will refer to a small business entity as presently defined in the tax law ie carrying on business with an aggregated annual turnover of less than \$2 million.
- The existing provisions contained in the Bill which is currently before parliament are intended to continue to apply to businesses which are not "small businesses."
- Example: A small business entity expending \$30,000 on 12 May 2009 to acquire an eligible asset which is installed ready for use on 1 July 2009 would obtain an additional deduction of \$15,000 in the 2009-10 year. This presumes the legislation is ultimately enacted in accordance with the terms of the budget announcement.

This concession represents a real benefit to business and has already had an effect on suppliers of capital equipment. We know of some motor dealers who are now experiencing a shortage of new car stock!

There are some planning opportunities with this and as 31 December approaches, those who are intending to avail themselves of the concession but aren't yet ready to do so, should contact us for further advice.

### Entrepreneurs' Tax Offset – Income Testing Deferred

The family income test for the entrepreneurs' tax offset which was announced in the 2008/09 Federal Budget will be deferred for a further 12 months. This means the family income test will commence on 1 July 2009 instead of 1 July 2008.

The entrepreneurs' tax offset provides a maximum 25% tax offset against the tax liability for small business entities with annual turnover below \$75,000. Under the proposed family income test, the entrepreneurs' tax offset would begin to be phased out for singles with income of \$70,000 and families with income of \$120,000. The deferral of the income test will mean eligible small business will not have their entrepreneur's tax offset reduced in the 2008/09 year.

### New R&D tax credit

From 2010/11, the current R&D concession will be replaced by the R&D Tax Credit. The government will consult further on the eligibility criteria in developing legislation for the new tax credit. A consultation paper will be released in the next few months.

The new R&D tax credit will provide a 45% refundable credit for firms with an annual turnover of less than \$20m (ie equivalent to a 150% deduction). The credit will be available to small companies in a loss position,

with no limit on the level of R&D expenditure undertaken.

Businesses with a turnover of more than \$20m will be entitled to a 40% non-refundable credit (equivalent to a 133% deduction).

Companies undertaking R&D in Australia where the intellectual property is held offshore will also be able to access the 40% non-refundable credit.

As a transitional measure for 2009/10, the R&D expenditure cap for the existing R&D Tax Offset will be lifted from \$1m to \$2m.

The Premium Concession and International Premium tax offsets will be abolished.

### Aggregation of Identical Assets

The Government reiterated that taxpayers will also be allowed to aggregate the eligible expenditure on identical or substantially identical assets to meet the requisite investment threshold. The eligible expenditure on assets may also be aggregated if they form part of a set. Items may be regarded as a set if they are dependent on each other, marketed as a set, or designed and intended to be used together.

### Pay As You Go (PAYG) Instalments — Cash Flow Relief

The Government will provide cash flow relief for small business by reducing Pay As You Go (PAYG) instalments for the 2009/10 income year for all taxpayers who pay quarterly PAYG instalments based on their previous year's tax adjusted by GDP growth.

For the 2009/10 income year, the Government will reduce the GDP adjustment factor for calculating quarterly instalments under the GDP adjustment method from around 9% to 2%. This aligns the GDP adjustment rate with the expected consumer price index (CPI) for 2009/10 as forecasted

Deemed dividends –

### Amendments to Division 7A

The Treasurer has announced that the application of the Deemed Dividend Rules in Division 7A will be widened to capture the use of company assets by shareholders and associates. The intended tax law changes will apply from 1 July 2009 and will deem the use of company assets to be a payment, thereby the use of a company asset will fall within the operation of the deemed dividend rules.

Currently, the operation of Division 7A is limited to taxing payments, loans and other similar arrangements made or provided by a private company to its shareholders and their associates. Where a shareholder or their associate is provided with free or discounted access to assets of the company (such as accommodation or a boat), the use of the assets will only be taxed where the individual provided with access to the assets is an employee and the benefit is subject to fringe benefits tax.

This provided a planning opportunity whereby access to these assets was provided to shareholders and their associates who were not employees, thus avoiding the operation of the fringe benefits tax provisions.

To counter these arrangements, shareholders of private companies and their associates will be required to pay for the use of the assets (determined by market value rates). Where the asset is provided by the company for less than market value, the shortfall will be deemed to be a payment under the amendments to Division 7A. This means the shareholder or associate will be assessed on this amount as a deemed dividend.

In a further announcement, the Treasurer said the operation of Division 7A is to be tightened through a series of technical amendments. The forms of these amendments was not announced (they will be subject to consultation), although the Treasurer did point to amendments to ensure that corporate limited partnerships could not be used to avoid the operation of Division 7A. There have been a variety of schemes in the marketplace designed to avoid Division 7A through the use of corporate limited partnerships in substitution of a private company. Clearly, these planned amendments will seek to prevent these types of arrangements

From 1 July 2009, the non-commercial loan rules will be extended to payments by way of a licence or right to use real property and chattels. This will reduce the scope for private companies to allow their shareholders or associates to use company assets such as real estate, cars and boats for free or at less than arm's length value. Other technical amendments will be made to Div 7A of ITAA 1936, including to ensure that corporate limited partnerships cannot be used to avoid its operation.

### Review of foreign source income attribution regimes

Australia's foreign source income attribution regimes will be reformed with effect for income years on or after Royal Assent to the legislation.

These changes implement most of the recommendations of the Board of Taxation review of the attribution regimes. To implement the Board's recommendations, the government will:

- modernise the controlled foreign company (CFC) provisions and rewrite them into ITAA 1997
- repeal and replace the foreign investment fund (FIF) provisions with a specific narrowly-defined anti-avoidance rule
- repeal the deemed present entitlement rules, and
- amend the transferor trust rules to enhance their effectiveness and improve their integrity.

The government will consult on the implementation of these reforms.

## CGT: limited roll-over for fixed trusts

A limited CGT roll-over will be provided for assets transferred between trusts that have the same beneficiaries with the same entitlements and no material discretionary elements (ie fixed trusts), with effect from 1 November 2008. Typically, the transfer of assets from one trust to another would trigger a CGT taxing point.

As a result of this measure, trustees of eligible trusts will be able to defer the CGT consequences of the asset transfer until the receiving trust subsequently deals with the asset. This will allow eligible trusts to restructure without immediate CGT consequences. The measure will be accompanied by appropriate integrity rules.

## TFN requirements for closely held trusts

From 1 July 2010, the tax file number (TFN) withholding arrangements will apply to closely held trusts, including family trusts. Such trusts will need to withhold amounts from trust distributions at the top marginal rate if taxpayers have not provided their TFN to the trustee. The measure will not apply to income on which tax is directly payable by the trustee of the trust (eg income assessable to minors). Individuals who have tax withheld by trustees can claim a credit for that tax in their tax returns.

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## Special Disability Trusts — Changes to the Taxation of Unexpended Income and the CGT Main Residence Exemption

The Budget contains measures to ensure that the unexpended income of a Special Disability Trust (SDT) is taxed at the relevant beneficiary's personal income tax rates rather than automatically at the top personal tax rate plus Medicare Levy. These measures will have effect from the 2008/09 income year.

A Special Disability Trust is a trust established for succession planning by parents and immediate family members for the future care and accommodation needs of a person with a severe disability.

The Government will also extend the CGT main residence exemption to include a residence that is owned by a Special Disability Trust and used by the relevant beneficiary as their main residence, with effect from the 2009/10 income year.

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## Other superannuation and retirement measures

### Pension age to be increased to 67

The age pension age will be gradually increased to 67 years of age. The new pension changes will apply to new pension entrants from 1 July 2017, which will mean that it applies to people who are 57 years of age or younger on July 2009.

## Pension drawdown relief extended

The minimum drawdown amount for account-based pensions will be halved for the 2009/10 income year. This extends the current concession provided to self-funded retirees for the 2008/09 income year.

The Seniors Supplement payment will also be made available to certain self-funded retirees. Self-funded retirees who are eligible for the Senior's Health Card or the Department of Veteran's Affairs Gold card with Seniors Concession Allowance will be eligible for the annual payment of \$790.40 for singles and \$1190.80 for couples.

## Retirement incomes report released

The Australia's Future Tax System Review Panel has released its report into retirement incomes. The review supports the current three-pillared system with some minor amendments. The major recommendations of the review include:

- increasing the age pension age to 67 years
- maintaining the current superannuation guarantee threshold of 9%
- aligning the superannuation preservation age with the age pension age
- undertaking further examination into the concessional tax treatment for superannuation contributions and for salary sacrifice arrangements.

The final version of the panel's report will be released in December 2009.

Access to the concessions for assets acquired on the death of an individual will be extended to cover assets that have passed to a testamentary trust where the individual would have been able to access the concessions at the time of their death. This extension will apply to CGT events happening in the 2006/07 income year and later income years.

The provisions which treat certain distributions to entities connected with a private company as dividends will be excluded from applying to the small business CGT retirement exemption. This exclusion will apply from Royal Assent of the amending legislation.

This measure was introduced into Parliament together with the previously announced changes to the concessions on 19 March 2009.

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