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FEDERAL BUDGET REPORT 2017

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"This Budget makes the right choices to secure the better days ahead"

–

Scott Morrison

Introduction

First home savers, downsizers and small business are the winners in Treasurer Scott Morrison's second Budget – while taxpayers face an increase in the Medicare levy.

The following wrap looks at the main changes that will impact Australians as they are rolled out (and potentially repealed) over the next few years.

It should be noted that most measures are proposals only; legislation is still required to be passed with possible changes and clarification to be provided.

Budget Summary

The Budget targets Australia's big five banks, multinational tax avoiders, foreign workers and foreign resident investors, while making voter-friendly announcements relating to health, education (particularly schools funding), infrastructure spending and housing affordability. Support for companies is focused on small businesses. For example, last year's Budget measure allowing enterprises with an annual turnover of up to $10 million to immediately write off asset purchases of up to $20,000 has been extended for another year.

This follows the government's achievement in getting $20 billion of its promised $50 billion in company tax cuts passed by parliament. Companies earning up to $50 million will have their tax rate reduced from 30 per cent to 25 per cent over 10 years. While these represent welcome measures to help small businesses navigate the global economy, it is important that the same logic be applied to all companies. Mid-size businesses (MSBs) – defined as having an annual turnover of between $10 million and $500 million – play a central role in driving innovation and growth. Reversing a decade of deficits will require MSBs to perform their share of heavy lifting, and every effort should be made to give them a spur.

Unfortunately, the Budget has again excluded MSBs from the government's asset write-off initiative. MSBs may face a tighter lending environment due to the new levy on banks. They will also incur significant new financial penalties for hiring foreign workers – potentially hurting their ability to source vital overseas talent. On the positive side, while cutting funding to universities, the government has kept research and development incentives intact. Australia's company tax rate is not particularly competitive when measured against its major trading partners. This situation will only worsen if the Trump administration succeeds in reducing the rate in the United States to 15 per cent. Despite being stymied by the Senate, we believe the government's original company tax cut plan is worth supporting in full. This should form part of a comprehensive suite of measures, including more cuts to red tape and shifting reliance from income tax to the GST. Australia deserves a simpler, more modern tax system that drives long-term growth for all businesses.

Superannuation

First Home Super Saver Scheme Proposed effective date: 1 July 2017

From 1 July 2017, individuals can make voluntary contributions (e.g. salary sacrifice, personal tax deductible, and non-concessional contributions) of up to $15,000 per year and $30,000 in total, to their superannuation account to purchase a first home. These limits apply to each individual – that is, a couple combined can contribute up to $30,000 per year and $60,000 in total.

Voluntary contributions under this scheme must be made within existing superannuation caps. Withdrawals of the contributed amounts along with the deemed earnings will be allowed from 1 July 2018. The amount of earnings that can be released will be calculated using a deemed rate of return based on the 90 day Bank Bill rate plus three percentage points.

The withdrawals of concessional contributions and associated earnings will be taxed at the individual's marginal tax rates less a 30% tax offset. When non-concessional amounts are withdrawn, they will not be taxed, but we anticipate that the earnings will be taxed at the individual's marginal tax rates less a 30% tax offset.

The First Home Super Saver Scheme will be administered by the ATO, which will determine the amount of contributions that can be released and instruct superannuation funds to make these withdrawal payments. The ATO will also be responsible for administering compliance mechanisms to ensure that people purchase their first home after they withdraw from superannuation for their deposit.

Observation:

• This measure may assist singles/couples to accumulate a deposit for a first home quicker than through other forms of voluntary savings.

Superannuation - cont

Contributing the proceeds of "property-downsizing" to superannuation Proposed effective date: 1 July 2018

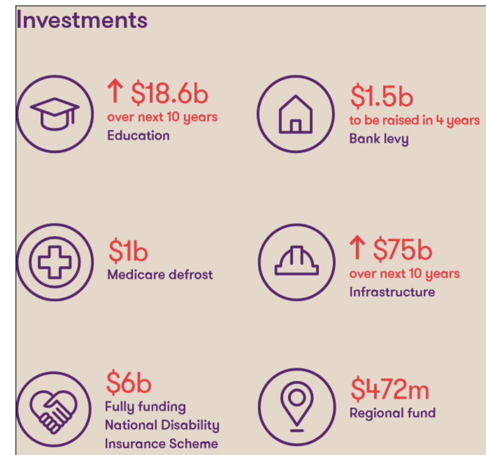
Currently, individuals aged 65 to 75 who want to make voluntary superannuation contributions must satisfy a work test. People over age 75 are generally unable to contribute to superannuation.

The Government proposes that from 1 July 2018, people aged 65 and over will be able to make a non-concessional contribution into their superannuation of up to $300,000 from the proceeds of selling their home, irrespective of their age, work status, and total superannuation balance.

Further, both members of a couple will be able to take advantage of this measure for the same home, meaning $600,000 per couple can be contributed to superannuation under this measure.

This measure will only apply to a principal place of residence held for a minimum of 10 years.

These contributions will be in addition to any other concessional or non-concessional contributions individuals are eligible to make.



Observations:

• Although the $1.6 million total superannuation balance assessment will not apply to these contributions, once the contribution is made, only individuals who have remaining transfer balance cap space available can convert their contributions into a retirement phase pension account where earnings are tax-free. • Importantly, there does not appear to be any special social security concessions associated with this measure. As such, social security clients may be adversely impacted.

Superannuation - cont

SMSF – Limited recourse borrowing arrangements (LRBA) Proposed effective date: 1 July 2017

The Government is proposing to include the outstanding balance of a LRBA in the calculation of a member's total superannuation balance (TSB).

Further, the repayment of the principal and interest of a LRBA from a member's accumulation account will result in a credit in the member's pension transfer balance account*****.

It's worth noting that these measures were previously outlined in Exposure Draft legislation released for industry consultation on the 27th April 2017 – submissions closed on the 3rd May 2017.

According to this exposure draft, existing LRBA's would not be impacted. That is, the exposure draft indicated that these proposed measures would broadly only apply for LRBA's entered into on or after the legislation receives Royal Assent.

*** The exposure draft legislation provided that a credit to a member's pension transfer balance account would only occur where loan repayments result in a transfer of value from accumulation to pension phase.**

Observations:
• Including the outstanding balance of an LRBA in the calculation of a member's TSB will impact on a member's ability to:
1. Make non-concessional contributions – where their TSB exceeds $1.6 million, or
2. Utilise the concessional contribution catch-up provisions (from 1 July 2018) where their TSB exceeds $500,000.

Personal Taxation

Marginal tax rates remain unchanged

Marginal tax rates are unchanged from 2016-17. As legislated, the Temporary Budget Repair Levy (TBRL) will expire on 30 June 2017. The TBRL is an additional 2% on the top marginal tax rate. Resident and non-resident marginal tax rates for 2017-18 are shown in the table below.

Tax rate applied	Current Thresholds
0%	$0 to $18,200
19%	$18,201 to $37,000
32.5%	$37,001 to **$87,000**
37%	**$87,001** to $180,000
45%	Above $180,000

Observations:

• The Low Income Tax Offset (LITO) remains unchanged which gives resident taxpayers an effective tax free threshold of $20,542 in 2017-18.

• Older Australians eligible for the Seniors and Pensioners Tax Offset (SAPTO) have an effective tax free threshold of up to $32,279 for singles and up to $28,974 for each member of a couple, also unchanged.

Increase to Medicare Levy

Proposed effective date: 1 July 2019 The Medicare levy is proposed to increase from 2% to 2.5% from 1 July 2019. The Medicare levy is still assessed on taxable income. The increase in the Medicare levy will be used to assist the funding of the National Disability Insurance Scheme (NDIS). Other tax rates which are linked to the top marginal tax rate (i.e. 47.5% following the increase) will also rise, such as the fringe benefits tax rate and the rate applied to employment termination payments in excess of the ETP cap (currently $195,000).

Increasing the Medicare levy low-income thresholds

The Medicare levy thresholds for low-income singles, families and seniors and pensioners will increase in the 2016-17 income year. The increases are based on movements in the consumer price index (CPI) so that low income earners are generally not liable for the Medicare levy. The threshold for singles will increase to $21,655. The family threshold will increase to $36,541 plus $3,356 for each dependent child or student. For senior singles and pensioners the threshold will increase to $34,244. The family threshold for seniors and pensioners will increase to $47,670 plus $3,356 for each dependent child or student.

Small Business & Corporate Tax

Instant asset tax write-off extension

Proposed effective date: 1 July 2017

The Government has announced a further extension to 30 June 2018 of the accelerated depreciation rules. These rules include allowing businesses with annual aggregated turnover of less than $10 million to immediately deduct purchases of eligible assets costing less than $20,000 where first used or installed ready for use by 30 June 2018.

Company tax rate reduction

Federal Parliament has now also finalised passage of legislation to reduce the company tax rate. The first step involves reducing (from 28.5%) to 27.5% for the 2016-17 income year the corporate tax rate for companies that are small business entities. That is, companies that carry on a business and have an annual aggregated turnover of less than $10 million (up from the existing under $2 million for this purpose). Other companies remain subject to the 30% corporate tax rate. The second step involves subsequent increases in this annual aggregated turnover threshold so that progressively larger companies that are carrying on a business will qualify for the 27.5% corporate tax rate. The legislation provides for the following increase in the annual aggregated turnover threshold that will attract the 27.5% corporate tax rate:

Income year	Aggregated turnover under ($ million)
2017-18	25
2018-19	50

Then, from 2024-25 the tax rate for these companies with an annual aggregated turnover less than $50 million will be progressively reduced as follows:

Income year	Company Tax Rate (%)
2024-25	27
2025-26	26
2026-27	25

Other

Pensioner Concession Card reinstated

Proposed effective date: 2017-18

Due to the assets test changes that came in 1 January 2017 some pension recipients were no longer entitled to a payment and as a result lost their Pensioner Concession Card (PCC). At the time those affected were issued with a Low Income Health Card and in some cases a Commonwealth Seniors Health Card. Although these cards provide clients with access to discounted medication under the Pharmaceutical Benefits Scheme, they don't provide all the ancillary benefits that the PCC provided. The Government will reinstate the PCC to those who lost their payment as a direct result of the 1 January 2017 asset changes.

Residential investment property – disallowance of deduction for travel expenses and limitation on deductible depreciation

From 1 July 2017, travel expenses incurred in inspecting, maintaining or collecting rent on residential investment properties will no longer be tax deductible. Residential property investors will continue to be able to deduct fees paid to real estate agents or other property managers for these services. In a separate proposal, depreciation deductions for plant and equipment in residential investment property will be limited to the actual expenditure incurred by the investor. Such fixtures include dishwashers and ceiling fans. This is an integrity measure designed to ensure that successive purchasers of a property cannot depreciate an asset beyond its actual cost. This measure will apply on a prospective basis with plant and equipment forming part of residential investment properties as at 9 May 2017 continuing to give rise to deductions for depreciation until either the investor no longer owns the asset, or the asset reaches the end of its effective life. Investors who purchase plant and equipment for a residential investment property after 9 May 2017 will be able to claim depreciation over the effective life of the asset. However, subsequent owners of the property will not be eligible to claim such depreciation allowances.

MATERIAL IN THIS REPORT SHOULD BE USED AS A GUIDE IN CONJUNCTION WITH PROFESSIONAL ADVICE.