

Technical Update

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The 2009 Federal Budget

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The Rudd Government handed down its second Budget on 12 May 2009. This is the first deficit Budget that Australia has seen in many years, with an expected deficit of \$58 billion.

A key focus of the Budget was to provide increases in the Age Pension, which has meant savings were needed in other areas. Superannuation strategies have taken a couple of hits to help fund these increases.

In the quest to provide real increases to retirees, some of the rules have become complicated and will create problems for financial planners. Software and calculators may not cater for all the scenarios.

This paper summarises the main Budget announcements changes that will impact on financial planning strategies. It should be noted, that all measures discussed in this paper (except for the personal tax cuts) are proposals only. Legislation is still required to be passed and further changes could be made. In some areas, further clarification is still required.

1. SUPERANNUATION

In November last year, the Government launched a review of the Retirement Income System. The Australia's Future Tax System (AFTS) Report on the retirement income system prepared by the AFTS Review Panel was released on Budget night.

Some measures (such as an increase in age pension age) were included in the Budget announcements, but the Panel has deferred most final recommendations until the final report in December to allow retirement incomes to be reviewed in the context of the broader tax-transfer system.

Some recommendations from the panel include:

- maintaining the superannuation guarantee at 9 per cent, not extending the superannuation guarantee to the self employed and retaining the \$450 per month threshold
- gradually increasing the Age Pension age to 67 years
- gradually aligning the age at which people can access their superannuation savings (the preservation age) with the increased Age Pension age
- improving the fairness and coherence of the pension means tests, possibly through a single test, and improve incentives to work beyond retirement age
- reducing the complexities resulting from the interactions between the tax-transfer system and the aged care sector
- maintaining tax assistance to superannuation but improving the fairness of concessions for contributions, including by broadening access to them, and considering whether the current cap on concessions is appropriate
- improving the ability of people to use their superannuation to manage longevity risk, and
- improving the awareness and engagement of individuals with the retirement income system.

a) Account-based pension minimum payments

Minimum payments from account-based pensions were halved for the 2008/09 financial year in response to the severe market downturns.

This concession will be extended for the 2009/10 financial year so that the minimum payments required from 1 July 2009 to 30 June 2010 will be:

Age	Percentage factor*
Under 65	2%
65 – 74	2.5%
75 – 79	3%
80 – 84	3.5%
85 – 89	4.5%
90-94	5.5%
95 or older	7%

* Based on the account balance as at 1 July 2009 or commencement date if commenced in the 2009/10 financial year.

The reduction in minimum payments also applies to term based allocated pensions.

Strategy implications:

Clients who have resources to generate income outside superannuation or can afford to live on lower incomes can choose to take a lower income payment. This may avoid the need to sell assets which have lost value.

b) Contribution caps

From 1 July 2009 the contribution caps for superannuation will be reduced as follows.

	Age	Cap amount
Concessional contribution cap	Under age 50	\$25,000
	Age 50 +	\$50,000
Non-concessional contribution cap	Under age 65	Up to \$450,000 (if bring forward rule triggered)
	Age 65 +	\$150,000

The reduced transitional cap for concessional contributions for people age 50 or older will apply until 30 June 2012. After that date, the standard cap of \$25,000 (or applicable indexed amount) will apply.

The \$25,000 concessional contribution cap is indexed to AWOTE and will increase in \$5,000 increments. The \$50,000 cap is not indexed.

The non-concessional contribution cap was planned to increase to \$165,000 from 1 July 2009 however this will no longer occur and the cap will remain at \$150,000 for 2009/10. It will only increase when the new lower \$25,000 cap is increased by indexation.

The existing 'grandfathering' arrangements that apply to certain members of defined benefit schemes in relation to the concessional contributions cap will continue. These arrangements will also be extended to certain persons who were members of defined benefit schemes on Budget night.

Strategy implications:

Review plans for clients who are salary sacrificing, including as part of a TTR strategy, to ensure they do not breach the cap. And don't forget, SG contributions are included in the concessional contribution cap.

c) Co-contribution

The co-contribution rate will be temporarily reduced for the next five years as follows:

Financial year	Co-contribution rate
2008/09	150%
2009/10	100%
2010/11	100%
2011/12	100%
2012/13	125%
2013/14	125%
2014/15 and later years	150%

The co-contribution income thresholds will not change and will continue to be indexed by AWOTE.

2. RETIREES

a) Age pension increases

From 20 September 2009, people who received an age pension, disability support pension, carer payment, wife pension or veteran income support pension will receive an increased payment.

The increased payments are delivered through a combination of an increase to the pension base rate plus a new Pension Supplement as follows:

	Total maximum increase (per week)	Portion paid as increase to base rate (per week)	Portion paid as Pension Supplement (per week)
Single	\$32.49	\$30	\$2.49
Couple (combined)	\$10.14	Nil	\$10.14

This brings the single rate of pension up to two-thirds of the combined couple rate.

Strategy implications:

A single person receiving the full pension and couples will receive the total maximum increase. Single part-pensioners will receive an increase between \$10.14 and \$32.49 depending on their pension entitlement under the income and assets test assessments.

b) Pension supplement

To simplify the payments made to pensioners, a new Pension Supplement will be created to replace the four current allowances of:

- GST pension supplement
- Utilities allowance
- Telephone/internet allowance, and
- Pharmaceutical allowance.

The increase in the Pension Supplement discussed above will be added to the current amounts for the four merged allowances so that from 20 September 2009, the Pension Supplement will be:

- \$1462.76 a year for singles (\$28.13 a week)
- \$2199.60 a year for couples (\$42.30 a week)

The Pension Supplement will initially be paid fortnightly. From 1 July 2010 pensioners can choose to receive around half of the new Supplement on a quarterly basis.

The Pension Supplement is added to the pension amount and the total payment is reduced by the income and assets tests. Once the payment is reduced to the minimum payment of \$790.40 a year for singles (\$15.20 a week) or \$1190.80 a year for couples (\$22.90 a week), the person is transferred to the Seniors supplement.

The Pension Supplement will be indexed twice a year by movements in the Consumer Price Index. This will occur in March and September at the same time as regular indexation of the base pension.

c) Seniors supplement

The Seniors Supplement will be available to self-funded retirees who are eligible for the Commonwealth Seniors Health Card or the Department of Veterans' Affairs Gold card with current Seniors Concession Allowance.

It replaces the existing payments of Seniors Concession Allowance and Telephone Allowance from 20 September 2009 and will be paid at the following rates:

- \$790.40 a year for singles (\$15.20 a week)
- \$1,190.80 a year for couples (\$22.90 a week)

Payments will be made quarterly.

d) Income test reduction rate

The pension income test reduction rate will increase from 20 September 2009 from 40 cents to 50 cents for each dollar of income above the income test 'free area'. This will reduce the maximum income thresholds to qualify for an age pension:

	Current rules – no pension is payable if assessable income exceeds	New rules – no pension is payable if assessable income exceeds
Singles	\$47,444*	\$38,693*
Couples (combined)	\$72,423*	\$59,229*

*Rates quoted are advised in Budget papers issued by the Government but the actual figures applicable at 20 September 2009 may vary due to indexation.

To complicate the calculations (but ensure all pensioners receive some payment increase), transitional rules will apply for existing part pensioners (as at 20 September 2009) if their pension would otherwise be reduced by this change.

If the person's pension would reduce on 20 September 2009, Centrelink will vary the calculations so that the person continues to receive the same pension (indexed) plus the \$10.14 per week increase for singles or couples combined. This concessional payment rate will continue until they are better off under the new rules.

e) Pension indexation

A new Pensioner and Beneficiary Living Cost Index (PBLCI) will be developed by the Australian Bureau of Statistics.

This will be designed to reflect changes in the cost of living for pensioners more accurately than the Consumer Price Index (CPI). For example age pensioner households are estimated to spend 21.1% of their household budgets on food, compared with 15.4% for other households.

From 20 September 2009, base pension rates will be indexed by the greater of CPI or the new PBLCI.

Pension rates will also continue to be benchmarked to Male Total Average Weekly Earnings, at the new increased rate of 27.7%.

f) Work and pension bonuses

Age and service pensioners will have access to a new work bonus to reduce the impact of employment income on their pension payments. Recipients of the Carer Payment and Disability Support Pension already have access to a Working Credit.

From 20 September 2009, only half of the first \$500 of employment income earned per fortnight will be assessed under the income test. Pensioners whose pension is paid under the transitional rules (described above in section 2e) cannot qualify for the work bonus unless they elect to move to the new rules.

The Pension Bonus Scheme will be closed to new entrants from 20 September 2009. People registered in the Scheme before 20 September will remain in the Scheme and claim a pension and their Bonus when they finish working.

Strategy implications:

Review clients who are over age pension age (65 for men and 63.5 for women) and still working to ensure they have registered for the Pension Bonus Scheme before 20 September 2009. Under current rates, the Pension Bonus could pay a tax-free lump sum up to \$35,000.

g) Commonwealth seniors health card

In last year's Budget the Government announced changes to the income test for the Commonwealth Seniors Health Card.

Under these changes, tax-free amounts withdrawn from superannuation or income streams would have been assessed as income from 1 July 2009. The good news is that the Government has decided not to proceed with these changes.

The income definition will be amended to only include salary sacrifice amounts.

h) Age pension age

The age pension age for both men and women will gradually increase from 65 to 67 by 2023. The Veterans' Service Pension age will remain at 60.

This change was inevitable as according to the United Nations, Australia has the fourth-highest life expectancy in the world. The United States, Germany, Norway, Denmark and Iceland are progressively increasing their pension age to 67, and the United Kingdom is increasing its pension age to 68.

The table below shows the affect of the changes.

Date	New age pension age	Affects people born	When group reaches new age pension age
1 July 2017	65.5	1 July 1952 to 31 December 1953	1 January 2018 to 30 June 2019
1 July 2019	66	1 January 1954 to 30 June 1955	1 January 2020 to 30 June 2021
1 July 2021	66.5	1 July 1955 to 31 December 1956	1 January 2022 to 30 June 2023
1 July 2023	67	From 1 January 1957	1 January 2022 to 30 June 2023

Strategy implications:

Anyone born after 1 January 1957 will not qualify for an age pension until they reach age 67. This may impact on retirement planning as clients may need to plan to work longer or to support themselves for the two extra years.

i) Aged care

The daily care fees paid in a residential aged care facility are linked to the rate of age pension. Therefore an increase in the age pension would normally increase the aged care fees.

The current basic daily care fee is set at 85% of the single age pension base rate. This will be reduced to 84% so the resident keeps an additional \$10.09 per week of pension payments.

Special arrangements will be put in place for part pensioners and self funded retirees currently in aged care who do not benefit from the full pension rise to protect them from any increase in the basic daily fee. These residents will not face any fee increase while in care.

New entrants from 20 September 2009 who also do not benefit from the full pension increase will have special transitional arrangements for a period of four years. These new residents will initially pay the same level of fees as currently paid by existing residents. Over the next four years their fees will gradually increase until they are paying 84 per cent of the base pension.

During this transitional period aged care providers will be compensated by government for any difference between the actual fee paid by new part pensioners and self funded retirees, and the daily fee paid by maximum rate pensioners.

3. MEDICARE AND HEALTH INSURANCE

a) Low income thresholds

Medicare is payable if taxable income exceeds thresholds announced in each year's Budget.

The table below shows the 2008/09 thresholds.

	No Medicare if taxable income is equal to or less than
Individuals	\$17,794
Individuals receiving a pension and under age pension age	\$25,299
Couple (combined)	\$30,025
Additional amount for each dependent child or student	\$2,757

b) Private health insurance

Australians have been encouraged to buy private health insurance through three measures. The current incentives are:

- Rebate on premiums – a rebate of 30%, 35% or 40% (depending on age)
- Medicare levy surcharge – 1% additional medicare levy is payable if taxable income exceeds \$75,000 for a single person or \$150,000 for couples/families and private insurance is not held
- Lifetime health cover – higher premiums are payable if health insurance is commenced over age 30

From 1 July 2010 changes are proposed to the rebate and surcharge rates for higher income earners.

Taxable income levels	Medicare levy surcharge rate	Private health insurance rebate		
		Up to age 65	Age 65 - 69	Age 70+
Singles				
< \$75,000	0%	30%	35%	40%
\$75,001 - \$90,000	1%	20%	25%	30%
\$90,001 - \$120,000	1.25%	10%	15%	20%
> \$120,001	1.5%	0%	0%	0%
Couples/families				
< \$150,000	0%	30%	35%	40%
\$150,000 - \$180,000	1%	20%	25%	30%
\$180,001 - \$240,000	1.25%	10%	15%	20%
> \$240,001	1.5%	0%	0%	0%

The income thresholds will be indexed each year by AWOTE.

Strategy implications:

Despite the loss of the rebate, higher income earners still have an incentive to buy private health insurance to avoid the Medicare Levy Surcharge.

Example	<p><i>Trevor's taxable income for 2010/11 is \$140,000. If he does not hold private hospital insurance for the whole year (with an excess no greater than \$500), he will pay Medicare Levy surcharge of \$2,100.</i></p> <p><i>If Trevor can purchase hospital cover for less than \$2,100 per annum it will be cheaper to hold the insurance than to pay the surcharge.</i></p>
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4. TAXATION

a) Personal tax rates

Legislation has already been passed for tax cuts effective from 1 July 2009. These tax cuts remained in the Budget. The personal tax rates for 2009/10 are:

Income range	Tax rate %
\$0 - \$6,000	0%
\$6,001 - \$35,000	15%
\$35,001 - \$80,000	30%
\$80,001 - \$180,000	38%
\$180,000 +	45%

In addition, the low income tax offset increases to \$1,350. This effectively allows an individual to earn \$15,000 before tax is payable.

Strategy implications:

With lower tax rates next year look for opportunities to defer income until after 1 July but claim deductions before 1 July. This may include prepayment of expenses,

b) Employee share schemes

Some employers offer employees the opportunity to buy shares or options in the company at a discount to market value. This discount is taxable under one of two options (chosen by the employee):

- The discount is taxable income in the year the shares are acquired, with the first \$1,000 tax-free (option does not apply to non-qualifying schemes), or
- Taxation of the discount can be deferred for up to 10 years (or when the shares are sold).

The second option will no longer be available for shares or options acquired after 7.30pm on 12 May 2009.

This means that all discounts will be assessed as taxable income in the year in which they are acquired. The \$1,000 exemption will be limited to employees with a taxable income of less than \$60,000 after adjustment for fringe benefits, salary sacrifice and negative gearing losses.

Strategy implications:

Employee share schemes no longer provide any tax advantages for employees with income over the \$60,000 threshold. These clients may wish to review arrangements to determine if they wish to continue purchasing shares under these schemes.

c) Deductions for non-commercial business activities

From 1 July 2009, high-income earners will not be able to deduct losses from non-commercial business activities (such as hobby farms) against other income.

The losses from these activities will only be deductible against the income from these activities if adjusted taxable income exceeds \$250,000.

In exceptional circumstances or where the losses are only temporary, the person can apply to the ATO for relief from these rules.

d) Entrepreneur's Tax Offset

Income testing of the entrepreneurs' tax offset (ETO) will be deferred until 1 July 2009 (instead of 1 July 2008 as announced in the 2008 Budget).

The ETO provides a 25% tax offset against the income tax liability for small businesses with an annual turnover below \$75,000. Under the income test, eligibility for the ETO will begin to phase out for singles with income of \$70,000 and families with income of \$120,000.

e) Use of company assets

Shareholders of private companies can currently use assets owned by the company (such as real estate, cars and boats) either for free or at less than arms' length value without fringe benefits tax applying. FBT only applies if the assets are used by an employee.

This rule will change on 1 July 2009 so that the value of the benefit will be taxable income to the shareholder.

Strategy implications:

Clients with private companies need to seek tax advice to determine the taxation impacts of assets used by a shareholder from 1 July 2009.

Example	<i>Richard is a shareholder of a private company that rents yachts. On weekends he can use the yachts for free. Under the proposed rules, Richard needs to pay market rates for the use of the yacht (which is taxable income to the company) or the value will be deemed an unfranked dividend to Richard.</i>
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f) Small business

In March, the Government announced tax concessions for small businesses on the purchases of eligible assets. These measures will be expanded further to allow a higher deduction.

Small businesses with a turnover of less than \$2 million can claim a bonus tax deduction of 50% (instead of 30%) of the cost of eligible assets. The assets must be purchased between 13 December 2008 and 31 December 2009 and installed by 31 December 2010.

All other businesses will receive a 30% deduction for eligible assets contracted for prior to 30 June 2009 and 10% for eligible assets that they commit to investing in between 1 July 2009 and 31 December 2009.

Strategy implications:

The increased tax deduction may provide small businesses with an incentive to invest in new capital items, such as computer hardware and business vehicles, and to make capital improvements to existing machinery and equipment.

g) Working overseas

Currently, Australians working overseas for 91 consecutive days or longer do not pay Australian income tax on their foreign employment income. This exemption aims to ensure that foreign employment income is not double-taxed but employees can obtain a tax advantage where the foreign country has a lower rate of tax than Australia.

Foreign earnings derived on or after 1 July 2009 by an Australian resident (individual) will only be exempt from income tax if they are employed as:

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

To avoid double-taxation, a tax offset will be available for any foreign tax paid on the foreign employment income.

Treasury will undertake stakeholder consultations concerning the legislation and administrative arrangements for these changes.

5. FAMILY PAYMENTS, CARERS AND DISABILITY

a) Family payments

The eligibility cut-off thresholds for family payments will not index over the next three years (until July 2012). Families at the upper end may lose eligibility as their income increases.

From 1 July 2009 to 30 June 2012, the eligibility income limits are:

- Family Tax Benefit Part B primary earner income threshold - \$150,000
- Dependency tax offsets - \$150,000, and
- Baby Bonus family income - \$75,000 (in the six months following the birth).

The upper income free area of Family Tax Benefit Part A will remain constant and depends on the age and number of children.

The Family Tax Benefit Part A lower income free threshold (currently \$42,559) and the Family Tax Benefit Part B secondary earner income threshold (currently \$4,526) will continue to be indexed annually by CPI.

Payment rates for Family Tax Benefit (Parts A and B) and the Baby Bonus will also continue to be indexed annually by CPI.

b) Paid parental leave

A government-funded scheme is planned to commence on 1 January 2011. It will provide the primary carer with 18 weeks post-natal leave, paid at the adult federal minimum wage (currently \$543.78 per week).

Employers will not be required to pay superannuation on paid parental leave entitlements.

To be eligible, the primary carer must earn less than \$150,000 per annum.

Non-working mothers will not benefit from the paid parental leave but will continue to be eligible for the Baby Bonus and Family Tax Benefits. Recipients of the paid parental leave scheme will not be eligible for the Baby Bonus or Family Tax Benefit Part B.

c) Carer and disability pension increases

From 20 September 2009, recipients of the Carer Payment and Disability Support Pension will receive payment increases of:

- \$32.49 per week for singles on the full rate, and
- \$10.14 per week combined for couples on the full rate.

This will be paid under the same basis as the increase in age pension payments.

d) Carer supplement

A new Carer Supplement of \$600 per annum will be paid to people who receive:

- Carer Payment
- both Wife Pension and Carer Allowance
- both Department of Veterans' Affairs (DVA) Partner Service Pension and Carer Allowance
- DVA Carer Service pension

It will also be paid to recipients of Carer Allowance at the rate of \$600 for each person they care for.

The supplement will be paid each six months. The first payment of the new Carer Supplement will be made to carers before July 2009. The regular payment will be made from 1 July 2010 onwards.

6. HOME BUYERS

The First Home Owner's Boost (FHOB) will be extended for an extra six months however, it will be reduced by half for the last three months of the extension period. This is available in conjunction with the First Home Owner's Grant (FHOG).

The available amounts are:

Contract entered into		FHOB	FHOG	Total grants
1 July 2009 to 30 Sept 2009	New home	\$14,000	\$7,000	\$21,000
	Established home	\$7,000	\$7,000	\$14,000
1 Oct 2009 to 31 Dec 2009	New home	\$7,000	\$7,000	\$14,000
	Established home	\$3,500	\$7,000	\$10,500

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