



## Federal Budget - May 2011



***The 2011/2012 Federal Budget held very few surprises, with several of the Henry Review recommendations included. The intention remains to return the Budget to surplus by 2012/2013, with a \$45.7B deficit currently estimated for 2010/2011.***

The major theme of this year's Budget has been on Australian health and education, with increased spending on hospitals, schools, teachers, as well as a substantial level of funds for mental health initiatives.

Many of the Budget announcements had been previously informed, and were merely official confirmation. We outline below some of the Budget announcements of relevance:

### **Superannuation**

Although there were a large number of superannuation changes announced, most of them have minor implications:

- Increasing the integrity of SMSFs via increased powers to the ATO to impose penalties on SMSF trustees who breach the legislation;
- To fund the increased integrity, the SMSF supervisory levy will be increased to \$180 pa (currently \$150 pa);
- Allowing taxpayers to request a refund if they exceed their concessional contribution cap by up to \$10,000. This measure would only be available for the first breach by a taxpayer;
- Continuing to extend the minimum pension drawdown relief for 2011/2012, but only by 25% rather than the 50% reduction as in previous years, with the return to normal limits for 2012/2013;
- Continuing the freeze on the indexation of the thresholds for the superannuation co-contribution;
- Requiring employers to disclose superannuation contributions on employees pay slips;

The Government further confirmed the implementation of superannuation changes that arose from the Henry Review, including:

- Increasing SG to 12% phasing in from 2012/2013;
- Retaining the \$50,000 concessional contribution cap for taxpayers aged 50 and over who have less than \$500,000 in superannuation from 1 July 2012;
- Providing a \$500 contribution to superannuation for low income earners whose adjusted taxable income is less than \$37,000.

## Trusts, Estates and SME Taxation

### *Changes to LITO for Unearned Income of Minors*

Currently unearned income of minors over \$416, such as distributions from trusts, is subject to tax at 46.5%, however tax on that income can be offset due to the application of the low income tax offset (LITO). This allows around \$3,300 of income to be distributed to minor beneficiaries each year without tax. From 1 July 2011, minors will not be able to offset LITO against their unearned income. For the current income year, the existing rules remain in place.

Accordingly, as from 1 July 2011, your Family Trust can distribute annually tax free to children and grandchildren under 18 as follows:

2010/2011	2011/2012
\$ 3,333	\$ 416

Although no mention was made, we would also expect that excepted trust income of minors, such as income from a family maintenance trust or testamentary trust, will continue to attract LITO.

### *Changes to the Taxation of Testamentary Trusts*

The current Tax Office practice of allowing a testamentary trust to distribute an asset of the deceased person without a CGT event occurring will be enshrined in the tax law.

More importantly, the income tax law in relation to deceased estates will also be rewritten using a principle based format and minor technical issues relating to deceased estates fixed. These changes will apply to CGT events happening on or after the day the legislation receives Royal Assent.

In addition, the Government plans to legislate to give the Commissioner a discretion to extend the two-year ownership period in which the trustee of a deceased estate or beneficiary of such an estate must dispose of their interest in the deceased's dwelling to access a full capital gains tax main residence exemption (or a more generous partial exemption).

### *Small Business Write-off for Motor Vehicles*

The government will allow small businesses to claim up to \$5,000 as an immediate deduction for motor vehicles, with effect for vehicles acquired from the 2012-13 income year. The remainder of the motor vehicle value will be pooled in the general small business pool (depreciated at 15 per cent in the first year and then 30 per cent).

Under the existing simplified depreciation rules for small business, motor vehicles are pooled in the general small business pool and depreciated at 30 per cent (15 per cent in the first year).

## Personal Tax Changes

### *Personal Tax Rates from 1 July 2011*

There were no Personal Tax Rate changes announced in last night's Budget. The Personal Income Tax Rates effective from 1 July 2011 will be the same as for 2010/2011 as follows:

From 1 July 2010 \$	Tax Payable \$
0 – 6,000	Nil+ 0%
6,001 – 37,000	Nil + 15% over 6,000
37,001 – 80,000	4,650+ 30% over 37,000
80,001 – 180,000	17,550 + 37% over 80,000
180,001 +	54,550 + 45% over 180,000

Note: Do not forget the additional Medicare Flood Levy will be imposed for the 2011/2012 year as follows:

Taxable Income	Medicare Levy	Flood Levy	Total
\$0 - \$50,000	1.5%	Nil	1.5%
\$50,000 - \$100,000	1.5%	0.5%	2.0%
\$100,000 Plus	1.5%	1.0%	2.5%

#### Other Announced Changes to Personal Tax

- The Government will abolish the Entrepreneurs' Tax Offset (ETO), with effect from the 2012-13 income year.
- The Government will phase out the dependant spouse tax offset (DSTO) for taxpayers with a dependant spouse born on or after 1 July 1971.

### Fringe Benefits Tax

#### Change in Motor Vehicle Fringe Benefit Rates

The 2011-2012 Federal Budget contained changes to the Fringe Benefits Tax (FBT) calculation rates for cars provided to employees as fringe benefits in contracts created after 10 May 2011. Presently the FBT rate of taxation for cars provided by employers when calculated under the statutory formula method are concessional such that the more kilometres travelled by the employee the less FBT is payable on the provision of that car.

This change only impacts cars for which the FBT calculation is based on the statutory formula method that are included in employment contracts after 10 May 2011.

For motor vehicles first included in contracts AFTER 7:30pm on 10 May 2011 the 20% Statutory Formula rate will be phased in over 4 years as follows:

Distance Travelled	Pre 10 May 2011 Contracts	Post 10 May 2011 Contracts			
		May 2011 to March 2012	April 2012 to March 2013	April 2013 to March 2014	April 2014 to March 2015
0 – 15,000	26%	20%	20%	20%	20%
15,000 – 25,000	20%	20%	20%	20%	20%
25,000 – 40,000	11%	14%	17%	20%	20%
40,000 +	7%	10%	13%	17%	20%

*If the vehicle's FBT is based on the actual costs of operation then this change would have no impact on the FBT payable on that vehicle.*

#### Fly in Fly Out Arrangements

The Government will extend the FBT exemption for domestic fly-in fly-out arrangements to cover Australian residents working in remote areas overseas. This measure will apply from 1 July 2009.

Currently, transport from an employee's usual place of residence to their usual place of employment for employees working in remote areas of Australia under fly-in fly-out arrangements is exempt from FBT.

In line with the current arrangements, the expanded exemption will **only** apply where employees cannot live anywhere other than in employer-provided accommodation at or near the work site, and no reasonable alternative accommodation is available.

## Corporate Tax

### ***Reforms to Promote Private Investment in Infrastructure***

The Government plans a new tax incentive designed to remove impediments in the tax system that discourage private investment in infrastructure projects.

The Government will establish special tax provisions for infrastructure projects designated to be of national significance. Losses generated by designated infrastructure projects will be exempt from the Continuity of Ownership Test (COT) and the Same Business Test (SBT) and will be uplifted at the government bond rate.

### ***Changes to Debt/Equity Rules***

The Government will amend the debt/equity tax rules to restrict the application of an integrity provision that deems an interest from an arrangement that funds a return through connected entities to be an equity interest under certain circumstances. The changes will ensure that this provision will only apply to arrangements where both the purpose and effect is that the ultimate investor has, in substance, an equity interest in the issuer company.

### ***Functional Currency Rules***

The Government will allow certain trusts and partnerships that keep their accounts solely or predominantly in a particular foreign currency to calculate their net income by reference to that currency.

### ***Company Loss Recoupment***

The Government plans to ameliorate the COT test by eliminating the need to trace through certain interposed superannuation entities.

There are also plans to remove technical deficiencies in the modified rules for widely held entities where:

- an entity is interposed between certain stakeholders and the loss company in certain circumstances;
- an interposed entity demerges;
- an interposed foreign entity issues bearer depository receipts; or
- a corporate change arising from the issue of new shares happens.

### ***Exploration will include Geothermal Energy***

- The Government will incorporate geothermal exploration into the wider definition of exploration, with effect from 1 July 2012.

### ***Tax Breaks for Green Buildings Deferred***

- The Government has deferred the start date of the Tax Breaks for Green Buildings measure to 1 July 2012 in order to allow more time to consider stakeholder proposals on the most effective way to implement the program.

## Tax Compliance

### ***Extension of the Director Penalty Regime to Cover SG***

With effect from 1 July 2011:

- the director penalty regime will be extended to superannuation guarantee amounts, making directors personally liable for their company's failure to pay employee superannuation;

- the ATO will be given the power to commence recovery against directors under the director penalty regime, without providing a 21 day grace period, for certain unpaid company liabilities that remain unreported after three months of becoming due; and
- in certain circumstances, directors and associates of directors will be prevented from obtaining credits for withheld amounts in their individual tax returns where the company has failed to pay withheld amounts to the ATO.

This is a major expansion of the director penalty regime.

### **Reporting Taxable Payments**

Certain businesses in the building and construction industry will have to report annually on payments made to contractors in the industry to the ATO, along with the contractor's ABN, with effect from 1 July 2012. This will allow data matching, thus reducing revenue loss due to non-reporting and underreporting of taxable income.

### **PAYG Instalments – Taxpayers Using the GDP Adjustment Factor**

The Government will reduce the GDP adjustment factor for PAYG instalment taxpayers who use the GDP adjustment method, from 8 per cent (which is the rate that would apply for the 2011-12 income year under the current law) to 4 per cent for the 2011-12 income year, half what it would normally be. The GDP adjustment factor for the PAYG instalment taxpayers increases the previous year's adjusted taxable income by the previous year's nominal GDP growth, to determine the tax instalments to be paid in the income year.

It is used by the overwhelming majority of taxpayers required to pay quarterly income tax instalments, mainly small businesses, but also some individual investors, certain trustees and small superannuation funds. This measure provides a significant cash flow benefit to such taxpayers who are required to remit less income tax instalments in 2011-12.

### **Our View**

As mentioned above, the Budget held very few surprises. However, it would have been preferable had further comments been made on other issues that require clarification:

- The treatment / classification of income for discretionary trusts – there are many outstanding issues in this regard that have created uncertainty, making it difficult to ensure that income is distributed correctly and in accordance with the family intentions;
- Despite the fact that the Government have announced a refund being available for those taxpayers who have exceeded their concessional contribution cap, this is not enough to remedy many of the contribution issues that taxpayers are currently facing.

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