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2011 Budget - Personal Finance Summary

The budget has provided a number of significant changes impacting on financial planning strategies. These have been outlined in this summary. The major changes include:

- The implementation of the flood and cyclone reconstruction levy for the 2011-12 financial year.
- Phase-out of the minimum draw down relief for superannuation pension holders will occur next year with minimums being 75% of the original rules and returning to the normal rates from July 1 2012.
- Some clarification of the operation of the higher superannuation concessional contribution cap for over 50s from July 1 2012. If a person is over 50 and has a superannuation balance of less than $500,000, they will be able to contribute $25,000 per year more than the standard concessional contribution cap.
- Extending the pause on indexation of superannuation co-contribution thresholds.
- Bringing forward the payment of the Low Income Tax Offset so that 70% of the offset is paid through the year and 30% paid through the end of year tax assessment whereas the current system sees only 50% paid through the year.
- Phasing out of the Dependent Spouse Tax Offset.
- Changes to the car fringe benefit rules by replacing the current statutory rates with a single rate of 20% that applies regardless of the distance travelled.
- Increasing the Medicare Levy low-income thresholds to $18,839 for singles and $31,789 for families.
- Removing a minor's eligibility for the low income tax offset on unearned income.
- Child Care Rebate will be able to be received directly into bank accounts on a fortnightly basis from 1 July 2011.
- Higher Education Scheme reduction in discounts from 20% to 10% on upfront student contributions and from 10% to 5% on voluntary payments of $500 or more.
- Disability Support Pension recipients will be able to work up to 30 hours per week and remain eligible for a part-pension for up to two years.
- Changes to assessment procedures for Disability Support Pension recipients.
- Increase in Family Tax Benefit Part A for families with 16 to 19 year old dependants in secondary education.
- Paid Paternity Leave implementation deferred until 1 January 2013.
- Abolishment of the Entrepreneur's Tax Offset with affect from 2012-13.
- Small businesses to be able to write off the first $5,000 for a motor vehicle purchase on top of last year's announcement that small businesses to be able to immediately write off asset purchases of less than $5,000 compared to the current limit of $1,000.

The following changes delivered since last year's budget have also been confirmed

- Age Pension new work bonus
- Education Tax Refund to cover school uniforms including optional and sport uniforms
- Baby bonus changes
- Deferment of a 50% discount commencing on the tax payable on the first $1,000 of interest income generated by bank, credit union and building society accounts along with income from bonds, debentures and annuity products until the financial year commencing July 1, 2012.

Each of the above items has been addressed in a little more detail in the following sections.

Implementation of the temporary flood & cyclone reconstruction levy

As previously announced, the Government will introduce a temporary flood and cyclone reconstruction levy from 1 July 2011 to contribute towards the cost of rebuilding flood and cyclone affected regions. This measure will apply only for the 2011-12 income year.

Those taxpayers with a taxable income in 2011-12 of $50,000 or less will not pay the levy. Taxpayers with taxable income between $50,001 and $100,000 will pay 0.5 per cent of their taxable income above $50,000. Taxpayers with taxable income over $100,000 will pay 0.5 per cent of their taxable income between $50,001 and $100,000 and 1.0 per cent of their taxable income over $100,000.

The Government has also provided some specific exemptions from the levy to anyone who:

- received an Australian Government Disaster Recovery Payment (AGDRP) for a disaster event in 2010-11;
- is directly affected by a National Disaster Recovery and Relief Arrangements (NDRRA) declared disaster in 2010-11 and would have met the AGDRP criteria; or
- is a New Zealand non-protected special category visa holder who received an ex-gratia payment from the Australian Government in relation to a disaster that occurred in 2010-11.

The impact of this levy is outlined in the following tables.

Taxable income	Rate	Flood Levy
($)	(%)	(%)
0 - 6000	0	-
6,001 - 37,000	15	-
37,001 - 50,000	30	-
50,001- 80,000	30	0.5
80,001- 100,000	37	0.5
100,001 – 180,000	37	1.0
180,001 +	45	1.0

Reduction in the minimum payment amounts for account based pensions 2011-12

The Government will phase out the pension drawdown relief that has been provided over the last three years. Minimum payment amounts for account-based, allocated and market linked (term allocated) pensions will be reduced by 25 per cent for 2011-12 and will return to normal in 2012-13. This will see the minimum draw downs for account based pensions (as a percentage of the account balance at the 1st of July or commencement of the pension):

Age of Beneficiary	2011-12 % factor	2012-13 % factor
Under 65	3.00	4
65 - 74	3.75	5
75 - 79	4.50	6
80 - 84	5.25	7
85 - 89	6.75	9
90 - 94	8.25	11
95 or over	10.50	14

Term Allocated Pension (TAP) payment factors will also reduce by 25% from normal levels with the exact details dependant on the individual arrangements for an account.

Strategy Thought
This may provide an opportunity for a range of pension account holders including the following scenarios:

- Those younger than 60 may be able to reduce pension draw downs to avoid paying tax on the withdrawal of taxable components whilst continuing to receive the tax free status on investment earnings of assets held within the pension. This will depend on salary sacrifice arrangements and the need to replace salary sacrificed income.
- Those older than 60 who do not need more than the new minimum pension payments will be able to withdraw a lesser amount of pension payments and thus preserve a larger balance.
- Those with TAPs can look to preserve the balance held in these accounts which will lead to improved access to Centrelink benefits in the future. This will depend on the ability to replace these pension payments from other sources.
- Those who have been drawing the reduced minimums will need to consider what to do with the increased level of payments.

Clarification of the operation of the higher concessional contributions cap for over 50s

The Government will set the higher concessional superannuation contributions cap for eligible individuals aged 50 and over with total superannuation balances of less than $500,000, due to apply from 1 July 2012, to $25,000 above the general concessional cap. This measure clarifies the operation of the higher cap for the over 50s which was introduced in the 2010-11 Budget, and means those eligible Australians over 50 will be able to contribute $25,000 more per year than other workers.

The general concessional contribution cap is set at $25,000. When it increases due to indexation, the higher cap will increase by the same dollar amount.

There remains a lack of clarity around the definition as to when and how the $500,000 balance will be calculated.

Strategy Thought
This provides an incentive for individuals who are aged 50 and above, or approaching this age bracket, to consider alternatives to keep their superannuation balance below $500,000 and thus remain eligible for the $50,000 of annual concessional contributions rather than the standard capped amount of $25,000, which will increase with indexation.

A key strategy to consider will be to implement superannuation contributions splitting strategies to direct superannuation contributions to a spouse who either has a much lower superannuation balance and / or who will not be able to take advantage of the increased concessional contributions threshold after turning age 50.

Careful consideration should also be given to where any personal (non-concessional) contributions are made so as to not push an individual's balance above $500,000.

Until the government provides clarification of the exact rules care should be taken implementing strategies.

Extending the pause on indexation of superannuation co-contribution thresholds

The Government will continue the freeze, for an additional year to 2012-13, of the indexation applied on the income threshold above which the maximum superannuation co-contribution begins to phase down. Under the superannuation co-contribution scheme, the Government provides a matching contribution for contributions made into superannuation out of after-tax income. The matching contribution is up to $1,000 for people with incomes of up to $31,920 in 2010-11 (with the amount available phasing down for incomes up to $61,920). This measure will continue to freeze these thresholds at $31,920 and $61,920 respectively.

Strategy Thought
Making a personal contribution to access the government co-contribution remains a worthwhile strategy for those who are eligible. However, eligibility has been tightened due to the non-indexation of the income thresholds.

Bringing forward the payment of the Low Income Tax Offset

The Government will increase the amount of the low income tax offset (LITO) that is delivered to low and middle income earners through their regular pay during the year from 50 per cent to 70 per cent of their total entitlements. The remaining 30 per cent of their LITO benefit will still be paid as a lump sum on assessment of income tax returns.

This adjustment will deliver up to $300 in more timely tax relief to low and middle income earners in the workforce. Individuals' total LITO entitlement in any one year remains unchanged. This measure will have effect from 1 July 2011.

Phasing out of the Dependent Spouse Tax Offset

The Government will phase out the dependent spouse tax offset (DSTO) for taxpayers with a dependent spouse born on or after 1 July 1971.

Taxpayers with an invalid or permanently disabled spouse, supporting a carer, or people who are eligible for the zone, overseas forces and overseas civilian tax offsets will not be affected by this change.

Changes to the fringe benefits tax rules for cars

The Government will reform the current 'statutory formula' method for determining the taxable value of car fringe benefits by replacing the current statutory rates with a single rate of 20 per cent that applies regardless of the distance travelled. This reform will remove the current incentive for people to drive salary-sacrificed and employer-provided vehicles further to increase their tax concession. This reform will apply to new contracts entered into after 7:30pm (AEST) on 10 May 2011, and will be phased in over four years.

Under the current statutory formula method, the calculated car fringe benefit decreases as the distance travelled by the vehicle increases. People can therefore increase their tax concession by driving their vehicle further.

<u>Strategy Thought</u>
Those who are affected by this change should reconsider their car leasing arrangements.

Increasing the Medicare Levy low-income thresholds

The Government will increase the Medicare levy low income thresholds to $18,839 for individuals and $31,789 for families, with effect from 1 July 2010. The additional amount of threshold for each dependent child or student will also increase to $2,919. The increase in these thresholds takes into account movements in the Consumer Price Index and ensures that low income families and individuals are not liable to pay the Medicare levy.

Removing a minors' eligibility for the low income tax offset for unearned income

The Government will remove the ability of minors (children under 18 years of age) to access the low income tax offset (LITO) to reduce tax payable on their unearned income, such as dividends, interest, rent, royalties and other income from property, with effect from 1 July 2011. This measure will discourage income splitting between adults and children.

Income earned by minors from work will still be eligible for the full benefit of the LITO. Unearned income of minors who are orphans or disabled, as well as compensation payments and inheritances received by minors will not be affected by this measure.

<u>Strategy Thought</u>
Those with family trusts will need to re-assess the disbursement of income generated by the trust each year and consider whether these changes to the taxation of income for minors change the use of a family trust structure.

Child Care Rebate to be payable directly into bank accounts on a fortnightly basis

The Government will provide families with the additional option of receiving Child Care Rebate (CCR) payments directly to their bank account on a fortnightly basis from 1 July 2011. This measure builds on the *Mid-Year Economic and Fiscal Outlook 2010-11* measure *Child Care Rebate — fortnightly payment*, which allowed families to receive CCR payments fortnightly as a fee reduction via their child care service.

Strategy Thought
Those eligible for the rebate should reconsider the most effective payment method.

HECS – reduction in discounts

The Government will, from 1 January 2012, reduce the following discounts applying to payments made under the Higher Education Contribution Scheme (HECS):

- the discount available to students electing to pay their student contribution up-front will be reduced from 20 to 10 per cent; and
- the bonus on voluntary payments to the Australian Taxation Office of $500 or more will be reduced from 10 per cent to 5 per cent.

Under HECS, students electing to pay their student contribution up-front will continue to receive a 10 per cent discount on the payment. Students choosing not to pay up-front can take out a concessional loan to pay their student contribution under the Higher Education Loan Program (HELP).

Under HELP, students accrue an outstanding debt which is repaid gradually when their assessable income exceeds a minimum repayment threshold. Students can also elect to make additional voluntary payments through the Australian Taxation Office to further reduce their outstanding HELP debt. Payments of $500 or more will now attract a 5 per cent bonus so that a payment of $500 would reduce an individual's outstanding HELP debt by $525.

Strategy Thought
This may deter the early payment of HECS & HELP debt especially if cash flow is tight. Keep in mind that the effective interest rate may see you better placed to use surplus cash flow to invest rather than paying back the debt. The decision whether to pay back in advance is very much dependent on your personal circumstances.

Disability Support Pensions - ability to work up to 30 hours per week and remain eligible for a part-pension for up to two years

The Government will allow all Disability Support Pension (DSP) recipients to work up to 30 hours a week and remain eligible for a part-pension for up to two years. This will allow recipients granted DSP under the 15 hour a week rule (that is, on or after 11 May 2005) to maximise their working hours without the suspension of their DSP entitlement. DSP recipients will still be subject to the application of the income test.

Strategy Thought
Those on a disability support pension and may be able to work may be more inclined to do so under these arrangements.

Changes to assessment procedures for Disability Support Pension recipients

The Government will bring forward the implementation of *more efficient and accurate assessments for Disability Support Pension and employment services* from 1 January 2012 to September 2011. From 3 September 2011, Disability Support Pension (DSP) claimants will need to provide evidence that they have tested their future work capacity by participating in training or work related activities. This activity test will not apply to claimants who are clearly unable to work due to, for example, profound disability.

The measure will purportedly improve assessments for DSP claimants who are currently required to undergo a Job Capacity Assessment to ensure that appropriate options for employment and income support are provided. Job Capacity Assessments will be refined to have a greater focus on a person's potential to work with appropriate capacity building and rehabilitation.

Increase in Family Tax Benefit Part A for families with 16 to 19 year old dependants in secondary education

The Government will improve the adequacy of Family Tax Benefit (FTB) Part A for dependent 16 to 19 year olds in full time secondary study. This will simplify the assistance provided to families with children in this age group, removing the need to choose between Youth Allowance and FTB.

FTB and Youth Allowance will be changed to:

- match the payment rates of FTB Part A for dependent 16 to 19 year olds in full time secondary study to the rates for 13 to 15 year olds. This will increase the level of support provided by FTB by up to $4,208 a year for 16 and 17 year olds, and up to $3,741 a year for 18 and 19 year olds;
- align the participation requirement for FTB Part B and the Multiple Birth Allowance with the existing FTB Part A participation requirement. This change will require 16 to 19 year olds to be undertaking full time secondary study, or be exempt from this requirement, to be eligible for these payments; and
- include all 16 to 19 year olds in full time secondary study for the purposes of calculating the Youth Allowance parental income test. This will ensure Youth Allowance recipients do not experience a lower rate of assistance as a result of siblings aged 16 to 19 years old in full time secondary study remaining in the FTB system.

Youth Allowance will continue to be available for 16 to 19 year olds who are independent, away from home or not in full time secondary study, and for people aged 19 years and older. All Youth Allowance recipients aged 16 to 19 on 1 January 2012 will have the option to remain on Youth Allowance.

Paid Paternity Leave implementation deferred until 1 January 2013

The Government will defer the implementation of Paid Paternity Leave by six months from 1 July 2012 until 1 January 2013. The measure will provide eligible working fathers, and other partners who are providing full-time care or sharing the child's care, with two weeks paternity leave paid at a rate equivalent to the national minimum wage for children born on or after 1 January 2013.

Abolishment of the Entrepreneurs' Tax Offset

The Government will abolish the Entrepreneurs' Tax Offset (ETO), with effect from the 2012-13 income year.

Small Business Asset Write-Off

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). The Government has previously announced that any new business asset worth less than $5,000 can be written off immediately from the 2012-13 income year.

<u>Strategy Thought</u>
Those small business owners considering discretionary capital purchases may look to delay these purchases until July 2012 if possible.

Changes announced between the last and current budget announcements

Age Pension new work bonus

The amount an age pensioner can earn before their pension is reduced will be increased. The new Work Bonus will allow age pensioners to earn up to $250 a fortnight without it being assessed as income under the income test. Under these changes, the Work Bonus can be 'annualised'. This means age pensioners will now be able to accumulate any unused amount of their $250 bonus every fortnight for up to 12 months. The unused amount can carry forward between years, up to a total of $6,500.

Strategy Thought
Those recipients of Age Pension entitlements may consider taking on or continuing part time work to increase income levels without reducing age pension entitlements or dipping into retirement savings.

Education Tax Refund to cover school uniforms including optional and sport uniforms

The Government will extend the Education Tax Refund (ETR) to include expenditure incurred on school uniforms from 1 July 2011. The ETR provides a refundable tax offset for 50 per cent of eligible education expenses, up to a maximum amount. For expenses incurred in 2009-10, the maximum amount of ETR was $390 for each eligible primary school student and $779 for each eligible secondary school student. In later years, these maximum amounts will increase in line with increases in the Consumer Price Index. Following the change, eligible expenses will include the costs of computers, computer software for educational use, school text books, stationery and uniforms.

Baby Bonus changes

The Government will provide eligible families with new babies $500 of their Baby Bonus entitlement upfront from 1 July 2011. The total amount of the Baby Bonus will remain unchanged at $5,294, meaning that the first fortnightly payment will be $868.77 with 12 subsequent payments of $368.77.

Deferment of the 50% discount on tax payable on the first $1,000 of interest income

The Government will defer the commencement of the 50 per cent tax discount for interest income announced in the 2010-11 Budget by 12 months and lower the cap on interest income that is eligible for the discount in its first 12 months of operation. Under the revised measure, the Government will provide individuals with a 50 per cent tax discount on up to $500 of interest income received in 2012-13, and up to $1,000 of interest

Summary of major strategy considerations

In a nutshell these are the possible strategy modifications arising from this year's budget:

- Reconsidering pension payment draw downs if looking to draw only the minimum allowed.
- Consideration of a superannuation contributions splitting strategy for those who might benefit from being able to receive extra concessional contributions into super from the age of 50 and also careful consideration of whose account to place personal contributions for couples.
- Users of car leases should reconsider their lease arrangements as a result of the proposed FBT rule changes.
- Users of family trusts to reconsider the use of the trust as a result of the removal of the LITO for minors.
- Recipients of Child Care Rebates should consider the most optimal method of payment as a result of the ability to receive payments directly into bank accounts each fortnight.
- Holders of HECS and HELP debt should reconsider the advance payment of debts according to their own circumstances as a result of the reduced discounts.
- Disability Support Pension recipients to consider whether taking on some part time work is in their interests due to the relaxed conditions around the impact of income on part pension payments.
- Small business owners to consider the timing of discretionary capital purchases.
- Age Pension recipients may consider taking on some or more part time work due to the new work bonus arrangements.

Concluding Comments

Overall the budget has not provided major changes in terms of personal finance outcomes. A widely held viewed is that this budget may actually be the prelude to a much more significant statement around the time of the introduction of the Carbon Tax and also once further details become available regarding the Mining Tax. There is also a major tax summit planned for later in the year.

One important conclusion from the budget is that there has not been significant tampering with the superannuation system. In previous years we have commented on concerns about the undermining of the confidence in the superannuation system through seemingly continual changes.

Investing through superannuation to provide for retirement is remains a very effective strategy with:

- Compulsory employer contributions
- Tax advantaged contributions and earnings through the accumulation stage
- Tax free superannuation withdrawals after the age of 60
- Income received tax free whilst in pension phase
- Minimal rules for withdrawing superannuation

This year's budget has also not seen the deferment of previously outlined plans:

- The increase in the SG contributions
- Tax rebate of superannuation contributions tax for lower income earners
- Improved accessibility to concessional contributions for those aged 50 and above
- SG contribution age limit increase from 70 to 75

Minimal change is actually a positive development and should improve confidence in the system moving forward.

This document has been prepared as a brief summary of the 2011 Federal Budget as it impacts on personal finances. It is a publication of A Clear Direction Financial Planning. It contains general financial information. Readers should check this information with a professional financial adviser before acting on any of the material contained in this document.