TAXWISE NEWS

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The 2011-12 federal Budget

The 2011-12 federal Budget handed down on 10 May 2011 was largely a ‘belt tightening’ by the federal government. Many of the announced measures were not a surprise, but are nevertheless important to consider.

You will need to take many of the measures announced in this Budget into account when calculating your **anticipated tax liability**, and also any **tax/estate planning and structuring** you were planning on undertaking in the next year or two. If you run a business and employ staff, or are an employee yourself, you should take particular notice of the changes to the **FBT rules**.

Set out below is a summary of the most significant measures announced in the Budget. However, many more changes were announced than are discussed here. In order to get the most specific advice for your circumstances, it is essential that you consult your tax adviser.

Tax rates

Tax rates are not going to change for the 2011-12 income year (as compared to the 2010-11 income year). This is the case for every type of entity, including individuals, companies and superannuation funds. Resident individual tax rates applicable for the 2010-11 and 2011-12 income years are set out following for your reference.

Taxable income	Tax on this income
$1–$6,000	NIL
$6,001–$37,000	15c for each $1 over $6,000
$37,001–$80,000	$4,650 plus 30c for each $1 over $37,001
$80,001–$180,000	$17,550 plus 37c for each $1 over $80,001
$180,001 and over	$54,550 plus 45c for each $1 over $180,000

However, if you are an individual, your effective tax rate will go up in the 2011-12 income year due to application of the once-off flood levy.

The flood levy will not be payable by taxpayers in flood-affected areas and taxpayers who have taxable income of less than $50,000 in the 2011-12 income year.

However, taxpayers with taxable income of between $50,001 and $100,000 will be required to pay 0.5% of their taxable income, and individuals who have taxable income greater than $100,000 will be required to pay 1% of their taxable income. This means that,for the first time in many years, you should consider trying to ensure that as much of your income falls in the 2010-11 income year as possible. You should, in this regard, seek tax advice specific to your circumstances.

Changes to offsets and rebates

The federal government announced changes to the operation of a number of offsets and rebates in this Budget. Some of these changes are effective as of Budget night. You should consider the application of these changes to your circumstances closely and carefully.

- From 10 May 2011, the **dependent spouse rebate** will be phased out for spouses aged less than 40 years of age. As of 10 May 2011, any individual with a spouse born on or after 1 July 1971 will not be eligible for this rebate.

- The low income tax offset (LITO) is a tax rebate for individuals on lower incomes. From 1 July 2011, **the LITO will increase from 50% to 70% of total entitlements**. This will not lead to an increase in the total offset available, but will lead to an increase in the percentage of the tax offset that will be available throughout the year. The rest of the tax offset will still be available as a cash lump sum at the end of the year.

- From 1 July 2011, the ability of children under 18 years of age **(minors) to access the low income tax offset** to reduce tax payable on their unearned income (such as dividends, interest, rent, royalties and other income from property) will be limited. This change will have the effect of significantly reducing the amount of passive income that you can distribute to a child effectively tax free. Income earned by minors from work will still be eligible for the full benefit of the low income tax offset.

- From 1 July 2011, **self-education expenses will no longer be deductible against government assistance** payments of any nature. As a result, students who receive Youth Allowance will still be entitled to claim a deduction for expenses incurred in gaining that payment for the 2010-11 income year. The Commissioner of Taxation has previously determined that students who have incurred such expenses in the 2006-07 to 2009-10 income years but have not retained receipts to substantiate these expenses will be entitled to a deduction of $550 per income year. Such students can make higher claims if the claims can be substantiated.

- From 1 July 2011, families in receipt of Family Tax Benefit Part A will be eligible for an **advance of up to 7.5% of their annual Family Tax Benefit Part A** entitlement (up to a maximum of $1,000). As above, this will not change the total value of your entitlement, but will allow you to access it at an earlier time.

- **The Family Tax Benefit Part A and Part B supplements, and the family payment higher income thresholds and limits**, will effectively be held at their present levels for the next three years, that is, they will not be indexed as in the past. This change may have the effect of limiting or cancelling your entitlement to these benefits, depending on your circumstances.

- From 1 January 2012, the **eligibility for Family Tax Benefit Part A will be limited to children up to the age of 21 years**. This change may have the effect of limiting or cancelling your entitlement to these benefits, depending on your circumstances.

- From 1 January 2012, **students electing to pay their HECS student contribution up-front will have their applicable discount reduced from 20% to 10%,** and the bonus on voluntary payments to the ATO of $500 or more will be reduced from 10% to 5%. As such, you should consider whether reducing any outstanding HECS bills or settling any such fees incurred up-front for the remainder of the 2011 calendar year may be beneficial for you.

Companies

The most significant change to the taxation of companies in the coming years will be the **reduction of the company tax rate to 29% for the 2012-13 income year for small businesses, and in the 2013-14 income year for all other companies**. This change was announced in the 2010-11 Budget, and then again in the 2011-12 Budget.

A number of minor amendments were also announced in relation to the taxation of companies, including:

- Amendment of the company loss recoupment rules to make it easier for companies to satisfy the continuity of ownership test rules.

- Changes to the small business CGT concession rules to tighten these rules in relation to trusts and broaden the rules in relation to some small businesses.

- Changes to the application of the scrip-for-scrip CGT roll-over.

TAX TIP!

The exact effect of these changes on your business will depend on a lot of different factors. You should get detailed tax advice to ensure that you fully understand the relevant tax consequences.

Small business

The following changes are most likely to affect the operation of small businesses:

- Many taxpayers use the GDP adjustment method when paying PAYG instalments. This 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 The **GDP adjustment factor will be reduced from 8% (which is the rate that would apply for the 2011-12 income year under the current law) to 4%** for the 2011-12 income year. This is likely to result in a reduction of the amount of your income tax bill that you have to pay up-front via PAYG instalments. However, it will not affect your total tax liability, and it may mean that you will have to find more money to pay your final tax bill, to make up for the smaller instalments you will have paid.

- **The entrepreneur's tax offset (which is currently only available for a very small percentage of taxpayers) will be replaced by an instant write-off** for the first $5,000 spent by a small business on the acquisition of a motor vehicle on or after 1 July 2012. This change will give you access to the benefit from the acquisition of the motor vehicle at an earlier time but will not increase the total deductions available to you in respect of the vehicle. The write-off will also be of limited benefit if your business is in a tax loss position.

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Small business operators should get detailed tax advice to ensure that you fully understand the relevant tax consequences.

FBT

At the moment, if you do not use the log book method, the more kilometers you travel in an FBT year, the lower the amount of FBT that is payable.

This method will be **phased out over the next four years and replaced with a flat rate of 20%.** This means that taxpayers who travel more than 25,000 km in an income year will, in later income years, have a higher FBT liability as compared to under the current regime. Taxpayers who drive less than 25,000 km in an income year may be able to benefit from acquiring a car via salary sacrifice.

The 20% flat rate will only apply to new vehicle contracts entered into after 7:30 pm (AEST) on 10 May 2011.

Not-for-profit sector

This Budget saw a number of significant announcements in relation to the not-for-profit sector, including:

- Currently, a charity can conduct a business enterprise and make a profit so long as the profits are applied for the benefit of the charity. In this Budget, the government will clarify the law so that concessions are bestowed only in relation to those activities that directly **further a charitable institution's altruistic purpose**. The new rules will apply from 1 July 2011 onwards and will initially affect only new unrelated commercial activities of a not-for-profit that commence after 10 May 2011.

- **A plan to legislate a statutory definition of "charity".** If you are currently registered as an income tax exempt entity due to being classified as a charity, this change may lead to a change in your status (depending on the detail of the new rules). The federal government will consult on this new definition in the coming months.

- The government will be creating **a new Charities and Not-for-profits Commission** which will consider applications for charitable status for the purposes of income tax exemptions, input tax credit concessions and a range of other government benefits. Currently, the ATO makes such determinations in consultation with Treasury as relevant.

TAX TIP!

If you operate as a not-for-profit entity, you should seek specific tax advice to clarify how these changes might affect or restrict your activities.

Superannuation

A number of changes have been announced in relation to superannuation funds in this Budget.

The most significant of these is that certain eligible individuals will be provided the option of having **excess concessional contributions taken out of their superannuation fund** and assessed as income at their marginal rate of tax, rather than incurring excess contributions tax.

This option will assist taxpayers who have inadvertently contributed too much to their superannuation fund and are therefore liable for excess contributions tax at the effective rate of 46.5%. The new rules will apply in respect of the 2011-12 income year and onwards.

In addition, individuals aged over 50 years with total superannuation balances of less than $500,000 will have their **superannuation contributions cap set to $25,000 above the general concessional cap** from 1 July 2012 onwards in order to assist such individuals in **contributing greater amounts into superannuation to fund their retirement**.

Furthermore, the indexation applied on the income threshold above which the maximum superannuation co-contribution begins to phase down will be continued for an additional year to the 2012-13 income year.

Currently, 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 the 2010-11 income year. The amount of matching contribution then decreases as the income increases, up to $61,920. This measure will continue to freeze these thresholds at $31,920 and $61,920, respectively, for the next two income years.