

# Budget Review

## The road to recovery Budget?

**The Budget has been handed down forecasting a \$58 billion deficit in the next financial year.**

Perhaps the biggest surprise in Treasurer Swan's second Budget, is the absence of surprise. The major "nasties" have been telegraphed ahead, with the rumours proving to be uncannily accurate.

The cash deficit for 2009 - 2010 is forecast at \$57.6 billion. The largest "revenue" measure is the halving of the concessional super contribution limits. The Government's super co-contribution rates will also be reduced. Private health insurance will become significantly more expensive for "high income earners" with the stepped reduction in the rebate, matched by an increase in the rate of Medicare levy surcharge to protect against a flight from private health cover. And the tax cuts already legislated for 2009 and 2010 remain unaffected. No surprises here.

But the raft of diverse and seemingly inconsistent policy changes is the surprise. There are 20+ changes to tax and related laws (depending upon how you count them) - some revenue raising, some expenditure items - and it will take business (in particular) quite some time to work through the detail, and assess the implications. One thing is sure - Big Brother is back, and the tax compliance burden for business is set to soar.

Some of the mooted changes - company tax rates, dividend imputation, flow through companies - have not appeared, but this is to be expected; changes of this nature will be held over until the end of the year, for

consideration in the Henry Review report. But there were a number of changes announced from other reviews - R&D, financial services industry initiatives, Board of Tax recommendations - which will require consideration by affected industry sectors. Quite a grab bag.

And the welfare sector will have its own need to review and consider, the release of the Harmer Pension report setting out the proposed new platform for future welfare support. Be prepared to continue working - the aged pension age is set to be extended to 67 (but not until 2017).

The overall tenor of the Budget is stimulus and jobs protection; but it is difficult to know how many truly new initiatives are aired in the Budget, as opposed to the repackaging of prior announcements. This will be funded by anticipated net Government debt accruing to some \$189 billion by 2012-13. This represents 13.6% of GDP, and carries an annual interest cost of \$7.6 billion. The Government anticipates the Budget returning to surplus in 2015-16.

This Budget, with so many changes and different "dates of effect" will require close analysis. It is one where the devil will be truly in the detail. The summary items that follow aim to alert you to changes of relevance; for more detail, please call your RSM Bird Cameron advisor.

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### Budget Action checklist

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To help guide you through our Budget review we have used the following colour coding:



Urgent action



Medium term action



Long term action

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## Business tax measures

### Foreign company, trust and investment attribution provisions

#### Summary

It is universally accepted that Australia's Controlled Foreign Company, Foreign Investment Fund and Transferor Trust provisions impose excessive compliance burdens on those Australian's with foreign investments relative to the tax revenue these provisions collect. The Government has announced that these provisions will be either repealed or replaced by modernised provisions that both reduce compliance burdens and improve their integrity.

#### Action - Long term

No date has been scheduled for the introduction of these proposed new measures and the Government has announced a consultation process in respect of these reforms. Taxpayers are therefore unlikely to be impacted by or benefit from this announcement for some considerable time.

### Small Business and general business tax break

#### Summary

The Government has announced an additional and extended bonus deduction of 50% for the acquisition of new eligible assets by Small Business between 13 December 2008 and 31 December 2009. This represents an extension of the previously announced acquisition deadline of 30 June 2009. This tax break will apply to Small Business with turnover of less than \$2 million.

The asset must be installed ready for use by 31 December 2010 (previously 30 June 2010).

The previously announced 30 % and 10% bonus deduction will apply to all other businesses.

#### Action - Urgent

This measure is clearly aimed at Small Business investment in new capital assets. Consider the timing of acquisitions to maximise the allowance.

The extended acquisition time does not to apply to non Small Business. Investment by these entities will still need to be made by 30 June 2009 (and installed by 30 June 2010) to access the 30% bonus deduction.

### Division 7A amendments to use of assets

#### Summary

The Government will extend the rules deeming loans to shareholders to be dividends. The proposed amendments will cover circumstances where a shareholder (or associate) is permitted the use of company assets (such as real estate, car or boat) for less than market value consideration. Where these are provided to employees, fringe benefits tax will apply. The same benefits provided to shareholders under the current rules will be tax free. Under the proposed changes, the market value of the benefit provided to a shareholder will be deemed a payment, and therefore a dividend and taxable accordingly.

#### Action - Urgent

With the measures effective 1 July 2009, company assets used by shareholders free of charge will need to be reviewed to ensure the market value of the benefit is not deemed a dividend and taxable in the shareholder's hands.

## Business tax measures

### R&D tax credit boost

#### Summary

The Government claims that up to 5,500 small companies will benefit from a proposal to revamp and reinvigorate the existing research and development tax concession. From 2010-11 a new and simplified R&D tax credit will provide a 45% refundable credit to companies with annual turnover of less than \$20 million. This relates to a 45% refund of R&D expenditure when filing a tax return.

The credit will be available to loss companies and no upper limit will apply to the amount of qualifying R&D expenditure.

Companies with turnover of greater than \$20 million will be entitled to a 40% non-refundable tax credit, even if the intellectual property is held offshore.

As a transitional measure, for 2009-10, the maximum R&D spend entitled to the R&D Tax Offset will be lifted from \$1 million to \$2 million.

#### Action - Medium term

Consider whether the new regime will benefit entities not previously entitled to R&D concessions. Companies accessing the R&D Tax Offset should review their qualifying expenditure to take advantage of the transitional cap increase.

Companies might consider deferring R&D projects to 2010-11 to access the proposed changes.

### Off-market share buy-backs

#### Summary

The Government has said it will amend the tax treatment of off-market share buy-backs. These have proved to be an effective way to manage the return of capital to shareholders in recent years. Existing tax anti-avoidance rules add time and costs to the implementation of a share buy-back.

Among the potential implications of the proposed changes are:

- Less compliance and more certain outcomes for companies and shareholders.
- Formula based debits to company franking accounts.
- Denial of notional capital losses to participating shareholders in listed company buy-backs.
- To introduce a regime that sets out the income and capital components of the buy-back proceeds.

#### Action - Medium term

Flexible outcomes are achievable under existing share buy-back rules, but more certain outcomes with reduced compliance costs should be achievable under the proposed new share buy-back rules.

### Deferred compensation schemes - dead

#### Summary

The current tax treatment of shares and options issued to employees under an employee share scheme will change from Budget night.

Currently, if an employee is granted shares or options under a "qualifying" share scheme, the employee may elect to be taxed on the "discount" in the income year or defer the taxing point until the cessation time (such as when the employee disposes of the shares). Whereas, if the employee is granted shares or options under a "non-qualifying share" scheme the employee would be taxed on the "discount" in the year of grant.

Any options or shares issued after 7.30pm on Budget night will have the "discount" taxed in the grant year. This ensures that all forms of remuneration are taxable in the year received. Separately, the current \$1,000 up front tax exemption will be limited to employees with adjusted taxable income (after adjustment for fringe benefits, salary sacrifice and negative gearing losses) of less than \$60,000.

#### Action - Urgent

As a result of these new measures all employee share and option plans will need to be reviewed to ensure that the plans remain viable incentives. As the tax liability will arise in the year the shares or options are granted it would be inappropriate to restrict the employee from selling the shares until a later tax year.

## Business tax measures

### CGT Election for Managed Investment Trusts

#### Summary

With effect from the 2008-09 tax year, Managed Investment Trusts (MITs) will be able to make an irrevocable election to apply the CGT provisions to tax their disposal of assets (comprising shares, trust units and real property). MITs taxed as companies will be unable to make the election. Resident investors who receive eligible gains distributed by MITs will be eligible for CGT discounts. Non resident investors will be exempt from eligible gains distributed by MITs except where the gains are realised from the disposal of taxable Australian property.

#### Action - Urgent

MITs prima facie eligible to make this CGT election should immediately start considering the full implications of doing so. There could be negligible time between when these provisions are enacted and the date MITs pay their 2009 income distributions to investors.

### Uniform Capital Allowances

#### Summary

A large number of "technical" amendments are proposed to be made to the uniform capital allowance (UCA) provisions. The budget forward estimates provide for no income or expenditure arising from the proposed UCA measures. Companies operating in capital intensive industries such as the mining, petroleum and manufacturing sectors will be keen to examine the detail of these measures, (most should be beneficial to taxpayers) and/or to participate in the consultation process to assist with the development of legislation.

#### Action - Long term

The proposed consultation process will ensure a reasonably lengthy lag in the enactment of the UCA amendments.

### Snap-shot of key budgetary and economic projections

Projected budget deficit	2008-09	\$32.9 billion
Projected budget deficit	2009-10	\$57.6 billion
Budget deficit as a % of GDP	4.9%	
Real GDP	(.5%)	
Unemployment rate	8.25%	
CPI	1.75%	

## Personal tax

### 2010 and 2011 individual tax rates - resident of Australia

The legislated personal income tax cuts for 2009 and 2010 have been confirmed.

#### Tax rates from 1 July 2009

Taxable income	Tax on this income
\$0 - \$6,000	Nil
\$6,001 - \$35,000	15c for each \$1 over \$6,000
\$35,001 - \$80,000	\$4,350 plus 30c for each \$1 over \$35,000
\$80,001 - \$180,000	\$17,850 plus 38c for each \$1 over \$80,000
Over \$180,000	\$55,850 plus 45c for each \$1 over \$180,000

Low income tax offset \$1,350

#### Tax rates from 1 July 2010

Taxable income	Tax on this income
\$0 - \$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 \$37,000
\$80,001 - \$180,000	\$17,550 plus 37c for each \$1 over \$80,000
Over \$180,000	\$54,550 plus 45c for each \$1 over \$180,000

Low income tax offset \$1,500

### Restriction of non-commercial losses

#### Summary

A relatively small number of high net wealth individuals have been perceived to have unfairly claimed deductions for non-commercial business activities. These will be tightened.

The result is that taxpayers with an adjusted taxable income over \$250,000 (ignoring the business losses) will instead have deductions quarantined. They will only be able to offset future income from the business activity that gave rise to the losses. The existing rules will continue to apply to other taxpayers.

#### Action - Urgent

Taxpayers earning greater than \$250,000 will need to reconsider how these rules apply to non-commercial activities that are more likely to be in the nature of hobbies or lifestyle assets. Measure applies from 1 July 2009, with no proposed transitional arrangements or grandfathering.

## Personal tax

### Changes to the exemption for foreign employment income

#### Summary

Currently there is a general exemption from tax (section 23AG ITAA 1936) in Australia for foreign employment income that is earned overseas by an Australian tax resident provided the employment period is over 90 consecutive days (and the employee is exposed to tax in the foreign country). It is proposed this exemption will be removed and will only be available for income earned:

- as an aid or charitable worker employed by a recognised non-government organisation; or
- as a Government aid worker; or
- as a Government employee (e.g. defence or police force personnel deployed overseas).

#### Action - Medium term

Under new measures, employees who remain tax residents of Australia and earn overseas employment income will be taxed on this income in Australia at their marginal tax rate and will be entitled to foreign income tax offset.

For employees of Australian companies this may lead to an increased tax cost for the employer with the possible exposure to FBT on the provision of fringe benefits to those employees.

Those benefits may also be taxed in the overseas country, giving rise to double taxation (although consideration would need to be given to any applicable Double Tax Agreement).

### Paid parental leave

#### Summary

The Government will introduce paid parental leave, to parents for births and adoptions that occur on or after 1 January 2011.

The scheme will provide 18 weeks postnatal leave based on the federal minimum wage (currently \$533.71 per week)

To be eligible, a parent in paid work:

- must have worked continuously with one or more employers for at least 10 months of the 13 months before the expected date of birth or adoption;
- must have worked at least 330 hours in the 10 months (i.e. at least one day a week); and
- must have an adjusted taxable income of \$150,000 or less in the financial year prior to the date of birth or adoption of the child.

Employers will be required to administer the payment of the paid leave to employees, the Government will provide the funds in advance to the employer.

The scheme will be available to "workers" meaning that it will extend to the self employed, to casual workers and to contractors.

The payments will be taxable to the parent receiving the payment.

#### Action - Long term

Employers will need to consider other employment on-costs for any employee receiving these payments.

## Personal tax

### Private Health Insurance rebates and Medicare Levy

#### Summary

The Government will introduce from 1 July 2010 three new "Private Health Insurance Incentive Tiers" for single people with income of greater than \$75,000 and families with income greater than \$150,000 per annum.

	Current Surcharge thresholds (projected 2010-11)	Tier 1	Tier 2	Tier 3
Singles	\$0-\$75,000	\$75,000 - \$90,000	\$90,001 - \$120,000	\$120,001 +
Families	\$0-\$150,000	\$150,001 - \$180,000	\$180,001 - \$240,000	\$240,001+
Medicare levy surcharge	nil	1.00%	1.25%	1.5%
Private health insurance rebate				
Less than 65 years	30%	20%	10%	nil
65-69 years	35%	25%	15%	nil
70 years or over	40%	30%	20%	nil

For singles or families below these thresholds the current arrangements will remain.

#### Action - Long term

Individuals should consider their personal situation before the new measures are introduced from 1 July 2010, as Medicare Levy surcharge is applied on a daily basis.

## Superannuation changes

### Concessional contribution caps reduced

#### Summary

From 1 July 2009, the Government will reduce the superannuation concessional contributions cap to \$25,000 per annum (from \$50,000) and transitional arrangements for those aged over 50 will be cut to \$50,000 (reduced from \$100,000).

The transitional arrangements will cease from 1 July 2012 and for individuals aged over 50, the \$25,000 cap per annum will apply (or the indexed equivalent).

Non-concessional contribution cap will remain at \$150,000 per annum, for the year commencing 1 July 2009, and will not be indexed until after 30 June 2010 (it will be linked to six times the indexed value of \$25,000).

#### Action - Urgent

Individuals should consider maximising these caps before they expire at 30 June 2009. However, this is a financial decision and you should consult your financial planner before taking any action.



## Summary

### Action - Urgent

To be actioned by 31 August

Small Business and general business tax break

Division 7A amendments to use of assets

Deferred compensation schemes - dead

Restriction of non-commercial losses

Concessional contribution caps reduced

CGT Election for Managed Investment Trusts

Off market share buy-backs

Research & Development

### Action - Medium term

To be actioned by end of financial year

R&D tax credit boost

Off-market share buy-backs

Changes to the exemption for foreign employment income

### Action - Long term

To be actioned later

Foreign company, trust and investment attribution provisions

2010 and 2011 individual tax rates - resident of Australia

Paid parental leave

Private Health Insurance rebates and Medicare Levy

Uniform Capital Allowances

# Budget Review

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