Federal Budget 2017

Build it and they will come.

A brief assessment of the Federal Government's first Budget since taking office in 2016, and the second under the leadership of PM Turnbull and Treasurer Morrison. We look at the key issues impacting on your financial and future planning.

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Don't do drugs!

Let's try not to do them anyway? The 2017 Federal Budget is about making the "right choices" and being "fair and responsible". Which, translated into Treasurer-speak, means "I never want to hear anyone ever mention the 2014 Budget ever again...".

This time the Government has played a pretty straight bat (annual cricket reference – tick) and stuck closely to its pre-Budget announcement themes of infrastructure and housing affordability.

Superannuation and financial services came in for some interesting changes – some of which were expected and welcome. The Government is encouraging older people to downsize by allowing people aged 65 or older, including those over age 75, to contribute the proceeds of selling their home to super without the need to meet a work test. This will be effective from **1 July 2018**. The contribution of up to $300,000 (per individual) will also be exempt from contributions limits.

The Government has also devised a new plan to use super to fund deposits for first home purchases. From 1 July 2017, first home buyers will be able to make voluntary contributions to super – including salary sacrifice and deductible personal contributions – of up to $15,000 a year and $30,000 in total to provide a deposit on a first home. The Government has neatly sidestepped the problem of using super to fund a first home by not touching compulsory super contributions. This new plan will also get traction in the Senate, where Senator Nick Xenophon has long been a supporter of using super to pay for first homes. This appears to be a reasonable middle ground.

Some of the other changes were not so welcome – especially those affecting the major banks who will now be charged a levy of 0.06% a year on liabilities, starting from 1 July 2017. Foreign residents are also negatively affected as they will pay more in withholding tax and lose the CGT main residence exemption from 9 May 2017. On the revenue side, the Government has committed to fully funding the National Disability Insurance Scheme but will increase the Medicare levy from 1 July 2019 by 0.5% to pay for it. For those unemployed and receiving social security benefits, if you don't turn up to a scheduled job interview due to being 'under the influence of alcohol or drugs', your payments can be reduced and / or suspended.

On the whole, this is the 'Ginger Spice' of Federal Budgets (please don't cringe just yet). It is not Posh or Sporty, and Babies don't get a look in this time, but most importantly it certainly isn't Scary like 2014 (cue cringing).

We've summarised some of the key points from the Budget below, and follow this with a more in-depth explanation of some of those measures. Remember these are proposals only and are subject to the passing of legislation in a number of cases, which will remain challenging in the split Senate and should be discussed with us before making financial decisions based on them.

It is not an extensive summary covering every point, however those we feel most relevant. If there are any points that are of interest to you either covered below or not, we are more than happy to discuss what the Budget means for you and your family.

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Key Financial Planning Points Summary

The Key Changes – Superannuation.

First Home Super Saver Scheme

Effective 1 July 2017

From 1 July 2017, super can be used to assist with saving for a first home purchase. Up to $15,000 per year of voluntary contributions (which appears to capture both pre and post-tax) can be made to super, and then be available to withdraw for the purposes of purchasing a first home. A total amount of voluntary contributions of $30,000 can be made available under the scheme (so the $30,000 could be made over say 5 years, and if a couple, that's $30,000 each as long as you're both first home buyers). If salary sacrificing, these contributions must be made within existing concessional ($25,000 p.a.) contributions caps.

Contributions will also accrue 'deemed earnings' calculated at the 90-day bank bill rate plus three percentage points (i.e. 4.79% per year deemed earnings based on current rate). These earnings will be withdrawn along with the contributions when a home purchase is made.

On withdrawal, concessional contributions and deemed earnings will be taxed at the individual's marginal tax rate, less a 30 per cent tax rebate. First Home Super Saver accounts are created on an individual basis – meaning each member of a couple can have their own account. Importantly, the release of funds to purchase a home will **not** count as income for certain tests, such as HELP/HECS repayments, family tax benefits or child care benefits.

Aspect Wealth Advisers Comment

This measure replicates the thinking behind the abandoned First Home Saver Account scheme, but uses the existing super infrastructure to implement it. This scheme may also encourage younger people to engage with their superannuation well in advance of their retirement – hopefully driving more interest and attention to the ever-growing pool of default super accounts.

Contributing the proceeds of downsizing the home to super

Effective 1 July 2018

From 1 July 2018, people over age 65 who sell their family home, downsize and release equity, may have the opportunity to make a one-off contribution of up to $300,000 of the proceeds from the sale to their super. To qualify, the home which is being sold must have been their main residence for at least the previous ten years. If the home is owned jointly by a couple, each person will be able to access the $300,000 threshold.

The contribution appears to be similar to small business CGT contributions in that amounts contributed under this 'home downsizing cap' are exempt from the total super balance rules and are

not impacted by previous after tax contributions. Further, contributions under this cap will not be subject to age-based contribution restrictions (i.e. the 'works test'). Once made, the contributions will not provide any additional benefits to either the total super balance calculation or give rise to any adjustments to their transfer balance account.

It is important to note there are no provisions for social security means testing exemptions on these contributions – once made, the funds will be assessed as standard superannuation monies. This may prove too high a price to pay for many older Australians who would prefer to maintain their current level of social security benefits as opposed to releasing equity in their home to fund their retirement.

Aspect Wealth Advisers Comment

This is a fantastic change for older Australians who are willing to downsize their home, however, for most Australians who wish to 'age in place' or are concerned about their age pension entitlements this measure is unlikely to be enough to change their mind. The benefit will be especially an individual one and we strongly suggest talking to us before committing to selling your (or a parents) home. We can assist calculate the benefits and costs in relation to age pension, contributions, and tax. Also what this may mean longer term for moving into age care facilities.

Taxation

Disallow the deduction for residential rental property travel expenses

Effective from 1 July 2017, deductions for travel expenses related to inspecting, maintaining or collecting rent for a residential rental property will be disallowed. Additionally, the rules around claiming depreciation will change so that deductions for plant and equipment will only be allowed where an expense has actually been incurred.

Aspect Wealth Advisers Comment

An integrity measure to address concerns that many taxpayers have been claiming travel deductions without correctly apportioning costs, or have been claiming depreciation on assets for which they did not purchase. This measure will not prevent investors from engaging third parties such as real estate agents for property management services as these expenses will remain deductible.

Medicare Levy Rate

From 1 July 2019, the Government will increase the Medicare levy by 0.5% from 2% to 2.5% of taxable income to ensure the National Disability Insurance Scheme (NDIS) is fully funded and to future guarantee the Medicare system. Similar to the last increase in the Medicare levy, this further increase will only be used to fund the NDIS.

Low-income earners will continue to receive relief from the Medicare levy through the low-income thresholds for singles, families, seniors and pensioners. The current exemptions from the Medicare levy will also remain in place.

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It's a tax hike, no disputing that, but the consideration is that no-one will grizzle too much given what it is intended to fund. Other tax rates that are linked to the top personal tax rate, such as the fringe benefits tax rate, will also be increased. As a partial offset for very low income earners, the below measure attempts to counterbalance a little.

Medicare Levy low income thresholds

From the 2016/17 income year, the Government will increase the Medicare levy low-income thresholds for singles, families, seniors and pensioners to take account of movements in CPI so that low-income taxpayers will generally continue to be exempt from paying the Medicare levy.

The threshold for singles will be increased to $21,655. The family threshold will be increased to $36,541 plus $3,356 for each dependent child or student. For single seniors and pensioners, the threshold will be increased to $34,244. The family threshold for seniors and pensioners will be increased to $47,670 plus $3,356 for each dependent child or student.

Aspect Wealth Advisers Comment

A welcome event for low income earners given the rising Medicare Levy.

Extension of $20,000 instant assets write-off for small business

Effective date: availability extended by 12 months to 30 June 2018

Affected clients: Small businesses with a turnover of up to $10 million

The $20,000 instant asset write-off allowing a small business with turnover up to $10 million p.a. a tax deduction for the purchase of assets worth up to $20,000 in the year of purchase was due to end on 30 June 2017. This tax concession will be extended for a further 12 months to 30 June 2018.

Assets valued at $20,000 or more (which cannot be immediately deducted) can continue to be placed into a small business simplified depreciation pool and depreciated at 15 per cent in the first income year and 30 per cent each income year thereafter.

The reduced tax liability resulting from the tax deduction frees up cash flow for small business owners

which can be used to sustain and/or expand their businesses.

From 1 July 2018, it is proposed that the asset value thresholds will revert to the previous $1,000 limit.

HELP Debts

The Government will place the higher education sector on a more sustainable footing by revising the income thresholds for repayment of HELP debt, repayment rates and the indexation of repayment thresholds, effective from 1 July 2018. A new minimum threshold of $42,000 will be established with a one per cent repayment rate and a new maximum threshold of $119,882 with a 10 per cent repayment rate.

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Other Key Points in Detail

Below we are summarising several points that whilst introduced last year via the Budget, come into effect 1 July 2017. There are also a few measures that were planned but have since been abandoned.

Superannuation

Concessional (pre-tax) contribution cap reduced to $25,000

Effective 1 July 2017

The concessional contributions cap will reduce to $25,000 per annum for everyone regardless of age from 1 July 2017. Currently the concessional contributions cap is $30,000 for clients under age 50 and $35,000 for ages 50 and over.

From 1 July 2017, the Government will include notional (estimated) and actual employer contributions in the concessional contributions cap for members of unfunded defined benefit schemes and constitutionally protected funds.

For individuals who were members of a funded defined benefit scheme as at 12 May 2009, the existing grandfathering arrangements will continue.

Aspect Wealth Advisers Comment

The reduced concessional contributions cap of $25,000 does not apply until 2017-18. Clients should consider taking advantage of the current higher concessional cap of $30,000 (under age 50) and $35,000 (age 50 and over) in the 2015-16 and 2016-17 financial years.

Clients should review salary sacrifice arrangements and personal deductible super contributions to ensure they comply with the reduced concessional cap from 1 July 2017. May need to drip-feed contributions over a longer period in order to meet retirement goals as a result of the reduced concessional cap.

Catch-up concessional contributions

Effective 1 July 2017

Unused concessional contribution cap amounts will be able to be carried forward on a rolling basis over 5 consecutive years. This applies to unused cap amounts from 1 July 2017.

Access to unused cap amounts will be limited to individuals with a superannuation balance less than $500,000.

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The Government states this measure will allow those who take breaks from the workforce the opportunity to 'catch-up' if they have the capacity and choose to do so.

The measure will also apply to members of defined benefit schemes.

Aspect Wealth Advisers Comment

The ability to carry forward unused concessional cap amounts appears to apply to everyone who has contributed less than the concessional cap, not just those who take breaks from the workforce such as women and carers.

However, the reduction in the concessional cap to $25,000 pa will reduce the amount of concessional cap available to be carried forward.

Lifetime cap for non-concessional (post-tax) contributions

Effective 7.30pm (AEST) 3 May 2016

A lifetime non-concessional contributions cap of $500,000 was introduced effective Budget night last year, on 3 May 2016. This has been abandoned. After tax (non-concessional) contributions from 1 July 2017 will be limited to $100,000 p.a. per individual. This has been reduced from $180,000 p.a. per individual.

Remove contribution eligibility requirements for those aged 65 to 74

Effective 1 July 2017

The current work test that applies for people making voluntary contributions between age 65 and 74 last year was announced that it be removed. This has also been scrapped.

Introduce a $1.6 million superannuation transfer balance cap

Effective 1 July 2017

A cap will be introduced to restrict the total amount of superannuation that can be transferred from accumulation to pension phase to $1.6 million. Where an individual accumulates amounts in excess of $1.6 million, they will be able to maintain this excess in accumulation phase (where earnings will be taxed at the concessional rate of 15 per cent).

The cap will be indexed in $100,000 increments in line with the consumer price index.

Existing pension balances

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Members already in pension phase as at 1 July 2017 with balances more than $1.6 million will need to either:

• transfer the excess back into an accumulation; or

• withdraw the excess amount from their superannuation.

Individuals who breach the cap will be subject to a tax on both the amount in excess of the cap and the earnings on the excess amount similar to the tax treatment that applies to excess non-concessional contributions.

The Government has also confirmed commensurate treatment for members of defined benefit schemes will be achieved through changes to the tax arrangements for pension amounts over $100,000 from 1 July 2017.

Aspect Wealth Advisers Comment

This proposal will allow couples to have a combined pension balance of up to $3.2 million. How many people will this really impact? Not many. However, where most of a couple's superannuation savings are in one spouses name the $500,000 lifetime non-concessional cap will restrict a couple's ability to equalise their benefits to take full advantage of the transfer balance cap.

The requirement for members with balances already in excess of $1.6 million to either withdraw or transfer the amount in excess of the cap back to superannuation means that people with pension account balances in excess of $1.6 million have not been grandfathered from these changes.

Additional 15% contributions tax: threshold reduces to $250,000

Effective 1 July 2017

Division 293 tax, which is an additional 15% contributions tax payable by high income earners with income exceeding $300,000, will apply to those with income exceeding $250,000 from 1 July 2017.

The Government claims reducing the Division 293 tax income threshold will improve sustainability and fairness in the superannuation system by limiting the effective tax concessions provided to high income individuals.

It is important to note the definition of income for Division 293 purposes includes:

• Taxable income (including the net amount on which family trust distribution tax has been paid)

• Reportable fringe benefits

• Total net investment loss (including net financial investment loss and net rental property loss)

• Low tax contributions (non-excessive concessional contributions) including super guarantee, salary sacrifice and personal concessional contributions.

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Division 293 tax will apply to any low tax contributions that exceed the $250,000 threshold, assuming they form the top slice of income.

Transition to retirement pensions: removal of earnings tax exemption

Effective 1 July 2017

The tax-exempt status of income from assets supporting transition to retirement (TTR) income streams will be removed from 1 July 2017. Earnings will then be taxed at 15 per cent. This change applies irrespective of when the TTR income stream commenced, i.e. no grandfathering applies.

The Government states that reducing the tax concessional nature of transition to retirement income streams will ensure they are fit for purpose and not primarily accessed for tax minimisation purposes.

Aspect Wealth Advisers Comment

Taxing earnings on TTR income streams significantly reduces the tax effectiveness of strategies such as TTR and salary sacrifice. For clients aged 60 or over, TTR strategies may still be worthwhile as pension payments are tax free and allow tax effective salary sacrifice contributions. However, for clients under age 60, the tax benefits are minimal.

The taxation of earnings in pension phase will only apply to 'transition to retirement' income streams where the client has reached preservation age but not yet retired. Presumably income streams where the client has met a full condition of release such as retirement will continue to have the earnings tax exemption apply. Clients may look at arrangements involving ceasing a gainful employment arrangement over age 60 or ceasing work and declaring permanent retirement to meet the retirement condition of release.

Increased access to spouse superannuation tax offset

Effective 1 July 2017

The current spouse superannuation tax offset will be available to more people due to an increase in the spouse income threshold from 1 July 2017.

The income threshold for the spouse superannuation tax offset is increasing from $10,800 to $37,000.

A contributing spouse will be eligible for an 18 per cent offset worth up to $540 for contributions made to an eligible spouse's superannuation account.

Aspect Wealth Advisers Comment

Currently the spouse superannuation tax offset reduces where the spouse's income exceeds $10,800 and cuts out altogether when their income reaches $13,800.

If the same methodology applies, the tax offset would reduce where the spouse's income exceeds $37,000 and cut out altogether at $40,000.

The ATO will determine a person's eligibility for the LISTO and advise their superannuation fund annually. The fund will contribute the LISTO to the member's account.

Extend deductions for personal contributions

Effective 1 July 2017

Australians under 75 will be able to claim an income tax deduction for any personal superannuation contributions made to a complying superannuation fund up to their concessional cap. This effectively allows all individuals, regardless of their employment circumstances, to claim a deduction for their personal contributions up to the value of the concessional cap.

To access the tax deduction, individuals will need to lodge a notice of their intention to claim the deduction with their superannuation fund or retirement savings provider prior to lodging their tax return. These amounts will count towards the individual's concessional contributions cap, and be subject to 15 per cent contributions tax. Individuals can choose how much of their contributions to deduct however if they end up exceeding their concessional cap the deduction claimed on the excess contributions will have no effect as these amounts will be included back into the member's assessable income.

Individuals aged between 65 – 74 will need to meet the 'works test' to be eligible to contribution (i.e. work 40 hours in any 30-day period during the financial year. Work must be for 'gain', i.e. cannot be charity / volunteering unpaid work).

Aspect Wealth Advisers Comment

This announcement will dramatically simplify the eligibility requirements for a member to qualify to claim a deduction for a personal super contribution. The requirement to not be an employee during the financial year or to satisfy the 10% test will be replaced with a simple requirement to be under age 75.

The announcement also gives employees more flexibility and allows them to make personal deductible contributions in addition to super guarantee and salary sacrifice contributions, to use up any unused concessional cap at the end of the year.

Defined benefit scheme changes

Effective 1 July 2017

The Government has announced a range of reforms to the taxation of benefits paid from defined benefit schemes and constitutionally protected funds to ensure equitable treatment of members in these funds and accumulation.

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$1.6 million transfer balance cap

To broadly replicate the effect of the proposed $1.6 million transfer balance cap, the Government has announced that pension payments over $100,000 per annum paid to members of unfunded defined benefit schemes and constitutionally protected funds providing defined benefit pensions, will continue to be taxed at full marginal rates, however the 10 per cent tax offset will be capped at $10,000 from 1 July 2017.

For members of funded defined benefit schemes, 50 per cent of pension amounts over $100,000 per annum will now be taxed at the individual's marginal tax rate.

Personal income tax reduction

Effective 1 July 2017

The temporary budget repair levy will also drop off as planned at the end of this tax year. It is not a tax cut for those on the highest tax bracket, it was always slated as 'temporary' and the treasurer has confirmed its removal.

If you have any questions relating to the above information, or would like a more detailed assessment of how the Budget outcomes may impact on your particular circumstances, please do not hesitate to contact us. Additionally, if there is an area of the Budget not addressed above you may have questions on, we would be more than happy to discuss.

Sources:

- Treasury Budget Papers 2017
- FirstTech: 2017 Federal Budget Briefing
- IOOF Budget Update
- BT Budget Summary