



### ***Tax and Families***

Treasure Peter Costello has handed down his eleventh Federal Budget today. We have highlighted some of the main focus points that will be applicable to most of our clients.

There have been significant tax changes to the individual income tax rates as well as an overhaul of the Superannuation system. There has been no tax relief to the existing Company Tax rate of 30%, having said that there has been some change in the depreciation rates.

Mr Costello has used a \$60 billion revenue boom to deliver personal income tax cuts worth \$36.7 billion.

Costello's argues superannuation measures, encourage older workers to stay in the workforce and will dramatically simplify super.

While superannuation contributions will start to attract a 15 percent contributions tax and a 15 percent earnings tax, the present complex range of taxes and age based rules will be abolished for retirees aged 60 and over. There will be no tax on superannuation lump sums or super pensions from July 1 next year.

The superannuation changes are the most important reforms in a federal budget that sets up the

prices while being able to argue the budget does not put more pressure on interest rates because it maintains a surplus of \$10.8 billion, or 1.1 percent of gross domestic product.

However, the 2006 budget shows the size of the surplus will fall from \$14.8 billion and 1.5 percent of GDP in 2005-06 – meaning it will be providing a significant stimulus to the economy, putting pressure on interest rates.

Costello described the budget last night as one that would "build opportunity for the future"

The business lobby's long standing demands for tax reform may also be partially appeased by the decision to cut 2¢ from both top income tax rates – to 40¢ and 45¢ respectively – while also lifting the threshold at which the two rates cut in. when combined with already legislated tax cuts due to take effect on July 1, the 40¢ rate will cut in at \$75,001, instead of \$63,001, and the 45¢ rate will cut in at \$150,000, compared with \$95,000 under the present scale.

The combined cuts will slash the tax bill of a person on \$150,000 a year by 11 percent, or \$6200, but represent a cut of less than 4 percent, or \$510 a year, for a person on average weekly earnings.

In the form of major changes to the depreciation regime and small-business taxation worth \$3.7 billion over four years.

But business has also argued forcefully for changes that

effective marginal tax rates they pay on lost family benefits and extra income earned. Changes to the income-tax scale will lift the income level at which the 30 percent tax cuts in from \$21,600 to 25,000.

Costello argued last night that, combined with changes to income thresholds on the family tax benefits a payment and a lift in the low income tax threshold, disincentives to women joining the workforce would be reduced.

The government confronted the issue of the crisis of the shortage of child care places. The government opted last night to let the market decide how it met demand, removing all limits on the number of government funded child-care places, a move it hopes will help create an extra 25,000 place by 2009.

The budget papers reveal that the commodities boom, which continues to be underestimated by Treasury forecasts by almost \$60 billion for the 2005-06 to 2008-09 period, since the budget last year.

The government will spend almost \$45 billion of that extra revenue on the new round of tax cuts, as well as increased spending on defence, national security, families and the elderly.

Despite the significant impact on household budgets of the two rounds of cuts hitting pay packets on July 1, the economy is forecast to grow at a moderate pace of only about 3.25 percent next year, compared with 2.5 percent last year.

Higher interest rates and petrol prices are expected to keep moderating consumption spending in a heavily indebted household sector; housing itself continuing a gentle decline.

Almost half a million low- and middle-income families will qualify for higher family benefits when the Howard government lifts the income threshold at which the assistance declines. And 330,000 of these families will also receive another bonus as those with three dependent children become eligible for the large family supplement, previously available only to parents of four or more.

The changes will expand the tax benefit system to funnel \$28 billion next year to families with children, double the spending of ten years ago.

From July, these families will be able to earn an extra \$2500 a year before their FBT part A is reduced – a change that will cost the government \$993.3 million over four years.

In the budget last year, the government lifted the income threshold at which the FBT part A starts to decline, to \$37,500 for 2006-07 and has now announced it will lift it again, to \$40,000.

Lifting the threshold will deliver an increase of an average \$9.60 a fortnight in family tax benefits to more than 480,000 families who are earning between \$37,000 and about \$50,000.

The combined effect of tax cuts and the increase in the FBT threshold expansion of the large family supplement would give a single-income family earning \$40,000 with three children and extra \$2113 next year.

No change has been made to FBT part B which is targeted at single income families and has been criticised by Labor as delivering welfare to millionaires wives.

Extending the large family supplement will cost \$497 million over four years and will provide parents with about \$10 a

fortnight. The budget is supposed to make Australia more "female friendly." \$94 million has been embarked for next year to help welfare dependant mothers with childcare fees.

The government will also provide a tax-free bonus payment of \$1000 to people on the carer payment looking after some one with a disability, and \$600 to those on the carer allowance.

### **Superannuation**

The tax on superannuation payouts will be virtually abolished and the assets test on the pension will be relaxed under a plan which the federal government hopes will encourage more savings and make superannuation more attractive. But the reduced tax regime will not apply for retirees under 60 as part of a series of measure designed to keep people in the workforce longer.

On the majority of super payouts no tax will be paid from July 1 next year. It is estimated that the retirement income will average on a weekly basis of \$1000 by \$170. Investors in some public sector funds will still be required to pay tax, however it will be on a much lower rate than today.

Retirees once they reach the age of 65 will be allowed to delay drawing down their super and to make pre-tax super contributions until they are 75.

On the next financial year the reforms will cost \$1.6 billion rising to \$2.3 by 2009-10. The aim is to simplify the super system, making it easier to understand and more flexible.

A uniform cap of \$50,000 has replaced the variable limits on pre-tax super, allowing people under the age of 39 to sacrifice far more salary into super but having the amount which anyone over 50 can contribute.

Self employed people are being encouraged to invest in superannuation. This will allow them to claim super co-contributed for low- to middle-income earners and claim full tax deductions for contributions made up to an age based limit.

Couples will now be able to hold up to an extra \$275,000 in assets outside super due to the fact the asset test that cuts the age pension by \$3 a fortnight for every \$1000 above the prescribed asset limit will be halved.

The financial services industry has long lobbied for the removal of the 15 percent contributions tax superannuation, arguing that Australia is one of the few countries to tax its pensions at three stages – on contributions, earnings and benefits – before investors receive their money. But the government said removing the contributions tax would be more costly and increase the complexity of the retirement system.

People after the age of 65 will no longer be forced to take their superannuation and will be able to continue making contributions until they are 75.

The rules for pension and annuity will become more flexible to allow investors to decide how to receive their pension. Funds will no longer have to report on a range of tax and benefit payments made to members over the age of 65.

### **Business**

New rules have been created for tax deductions; example: a new computer to the value of \$4000 will be \$3000 after the first two years rather than \$2435 under the current law.

In the fringe benefits department, there is good news. Meaning that the tax rates on perks have been cut from 48.5 per cent to 46.5 per cent backdated to April this year. The cut will cost \$870 million over four years.

Evidence suggests that 200 per cent rate of the diminishing value is more appropriate in the world of technology that is advancing at a great velocity, than the current of 150 per cent.

*For any further information on the above please do not hesitate to Magdy Marcos at our office on (02) 9893 8600.*