

PERSONAL TAXATION

No change to personal tax rates; Budget deficit levy to end

The 2017–2018 Federal Budget contained no changes to the personal income tax rates and thresholds. This means that the 2% budget deficit levy on incomes over \$180,000 will not be extended beyond its initial three years, and will cease on 30 June 2017.

The tax rates for foreign residents for 2017–2018 will be the same as those for 2016–2017, except that the top marginal rate will be 45%, reflecting the removal of the 2% temporary budget deficit levy.

The currently legislated low income tax offset (LITO) rates have not changed.

Medicare levy increase to 2.5% from 1 July 2019

The Government will increase the Medicare levy to 2.5% from 1 July 2019 (up 0.5% from the current 2% Medicare levy) to ensure the National Disability Insurance Scheme (NDIS) is fully funded and to guarantee Medicare. Other tax rates that are linked to the top personal tax rate, such as the FBT rate, will also be increased.

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.

The increase in the Medicare levy is estimated to raise \$8.2 billion over the forward estimates, being the net impact across all heads of revenue, not just the Medicare levy. The Government said it will credit \$9.1 billion to the NDIS Savings Fund Special Account when it is established.

Low income thresholds for 2016–2017

The Medicare levy low-income threshold for singles will be increased to \$21,655 (up from \$21,335 for 2015–2016). For couples with no children, the family income threshold will be increased to \$36,541 (up from \$36,001 for 2015–2016). The additional amount of threshold for each dependent child or student will be increased to \$3,356 (up from \$3,306).

For singles eligible for the Seniors and Pensioners Tax Offset, the Medicare levy low-income threshold will be increased to \$34,244 (up from \$33,738 for 2015–2016). The family threshold for seniors and pensioners will be increased to \$47,670 plus \$3,356 for each dependent child or student.

Higher Education HELP changes confirmed

The Budget confirmed the announcement on 1 May 2017 by the Minister for Education and Training, Simon Birmingham, of the Higher Education Reform Package to take effect generally from 1 January 2018. See *Client Alert* for an overview of the key measures.

Tax free payments to child sexual abuse survivors

Redress payments under the Commonwealth Redress Scheme for Survivors of Institutional Child Sexual Abuse (the Scheme) will be tax exempt. The Scheme will commence in March 2018 and start receiving applications from 1 July 2018 from people who were sexually abused as children in Commonwealth institutions.

Changes to FTB Part A payments

The Budget confirmed that, from 1 July 2017, Family Tax Benefit Part A supplement payments will be reduced by \$28 per fortnight for each child who does not meet the Government immunisation requirements.

Changes to dollar income test taper

The Government will implement a consistent 30 cents in the dollar income test taper for Family Tax Benefit Part A families with a household income in excess of the Higher Income Free Area (currently \$94,316) from 1 July 2018. This will ensure that higher income families are subject to the same income test taper rates.

Proposed Part A rate increase not proceeding

The Government will achieve savings of \$1.9 billion over four years from 2017–2018 by not increasing the maximum rate of Family Tax Benefit Part A, which was announced as part of the 2015–2016 Mid-Year Economic and Fiscal Outlook.

A standard tax deduction for work expenses? Not in this Budget

Talk of allowing individual taxpayers a standard tax deduction for work-related expenses (WRE) has been around for more years than we may care to remember. However, despite much speculation before the Budget, it was silent on such a proposal.

The Henry Tax Review in 2010 recommended a standard deduction to cover work-related expenses and the cost of managing tax affairs to simplify personal tax for most taxpayers. Taxpayers should be able to choose either to take a standard deduction or to claim actual expenses above the claims threshold, with full substantiation. Then, in the 2010–2011 Federal Budget, the Government announced that it would provide individual taxpayers with a standard

deduction of \$500 for work-related expenses and the cost of managing tax affairs from 1 July 2012, to increase to \$1,000 from 1 July 2013. Of course, that did not proceed.

On 30 March 2015, the Treasurer released a tax discussion paper which also discussed WRE. Given the high proportion of taxpayers who incur a relatively low total value of legitimate WREs, the paper suggested a standard deduction could provide significant compliance savings. Rather than substantiating WRE expense claims with receipts, these taxpayers could “tick a box” to claim a standard deduction at a set amount. While it could deliver a simplicity benefit, the paper noted that a standard deduction would come at significant cost – people who do not currently have any WRE deductions could reduce their taxable income by the value of the standard deduction. The discussion paper was meant to be a precursor to a Green Paper covering tax options in the second half of 2015 and a tax reform White Paper before the 2016 Federal election, but neither eventuated.

Most recently, on 22 November 2016, the Treasurer asked the House of Representatives Standing Committee on Economics to inquire into and report on tax deductibility, specifically on the deductibility of expenditure by individuals in earning assessable income (including, but not limited to, a comparison with NZ and the UK), and deductibility of interest incurred by businesses. The Committee held a hearing in Canberra on 27 March 2017 (with a particular focus on WREs) but has not yet reported back to the Government. It heard that during the 2015 year, nearly \$22 billion in work-related tax deductions were claimed. These claims have increased by 21% over the past five years, and the ATO has expressed concern about the level of non-compliance in relation to WRE.

It has been suggested that a standard tax deduction of \$2,000 would be appropriate (the statistics reveal that is about the average of claims made). Perhaps taxpayers could be given the option of claiming the standard deduction or, if they wish to claim more, substantiating in full. Overall, any steps to help minimise tax compliance complexity and cost are welcome, but of course, revenue implications would have to be factored in.

So the idea of a standard tax deduction has received plenty of attention in recent years. A standard deduction would of course constitute a hit to the revenue, although it could be clearly quantified. Maybe for another time, or maybe not at all.

BUSINESS TAXATION

Major bank levy from 1 July 2017

The Government will introduce a major bank levy for authorised deposit-taking institutions (ADIs) with licensed entity liabilities of at least \$100 billion from

1 July 2017. The threshold will be indexed to grow in line with nominal gross domestic product.

The levy will be calculated quarterly as 0.015% of an ADI’s licensed entity liabilities as at each APRA mandated quarterly reporting date (for an annualised rate of 0.06%).

Liabilities subject to the levy will include items such as corporate bonds, commercial paper, certificates of deposit, and Tier 2 capital instruments. The levy will not apply to the following liabilities: additional Tier 1 capital and deposits of individuals, businesses and other entities protected by the Financial Claims Scheme.

The levy is expected to raise \$6.2 billion over the forward estimates period, net of interactions with other taxes (principally corporate income taxes). The Government believes this represents a fair additional contribution from Australia’s major banks and will assist with budget repair.

Government commits to remainder of 10-year package to reduce company tax rate

The Budget confirmed the Government’s intention to re-introduce the remaining elements of its 10-year Enterprise Tax Plan.

Legislative amendments already passed by the Senate will see the corporate tax rate reduced for companies with a turnover less than \$50 million. These Senate amendments are set to be approved by the House of Representatives as part of the Budget sittings. The Government said it remains committed to its 10-year Enterprise Tax Plan to eventually reduce the company tax rate to 25% for all companies.

In the 2016–2017 financial year, the reduced corporate tax rate of 27.5% will apply for businesses with an aggregated turnover of less than \$10 million; \$25 million turnover in 2017–2018; and \$50 million turnover from 2018–2019. This effectively implements the first three years of the Government’s plan.

As per the trajectory in the Budget, the corporate tax rate will also be further reduced in stages, starting from 1 July 2024, so that it will eventually fall to 25% by the 2026–2027 financial year for businesses with an aggregated turnover of less than \$50 million.

Small business measures

In addition to the reduced company tax rate, the Enterprise Tax Plan Bill includes measures to:

- increase the small business entity aggregated turnover threshold to \$10 million from 1 July 2016 – but the threshold for accessing the CGT small business concessions will remain at \$2 million; and
- increase the unincorporated small business tax discount from 5% to 16% over a 10-year period – the threshold for accessing the discount will be \$5 million (aggregated turnover).

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The increase in the small business entity aggregated turnover threshold will enable a greater number of businesses to access concessions such as the simplified depreciation and trading stock rules and a two-year (instead of four-year) review period for amending assessments.

Higher instant asset write-off threshold for small business extended

The Government will extend the current instant asset write-off (\$20,000 threshold) for small business entities (SBEs) by 12 months to 30 June 2018.

The threshold amount was due to return to \$1,000 on 1 July 2017. As a result of this announcement, SBEs will be able to immediately deduct purchases of eligible depreciating assets costing less than \$20,000 that are acquired between 1 July 2017 and 30 June 2018 and first used or installed ready for use by 30 June 2018 for a taxable purpose. Only a few assets are not eligible for the instant asset write-off (or other simplified depreciation rules), for example horticultural plants and in-house software.

Assets valued at \$20,000 or more (which cannot be immediately deducted) can continue to be placed into the general small business pool (the pool) and depreciated at 15% in the first income year and 30% each income year thereafter. The pool can also be immediately deducted if the balance is less than \$20,000 over this period (including existing pools).

The instant asset write-off threshold and the threshold for immediate deductibility of the balance of the pool will revert to \$1,000 on 1 July 2018.

Note that when the SBE changes in the *Treasury Laws Amendment (Enterprise Tax Plan) Bill 2016* receive assent, the aggregated turnover threshold for a SBE will increase to \$10 million (from 2016–2017).

Accordingly, SBEs with aggregated turnover between \$2 million and \$10 million will benefit from the \$20,000 instant asset write-off concession.

Suspension of lock out rules extended

The suspension of the “lock out” rules for the simplified depreciation regime will be extended by 12 months until 30 June 2018. The “lock out” rules prevent SBEs from re-entering the simplified depreciation regime for five years if they opt out.

CGT small business concessions: restricted to assets used in business

The Government will amend the small business CGT concessions to ensure that the concessions can only be accessed in relation to assets used in a small business or ownership interests in a small business.

Division 152 of the *Income Tax Assessment Act 1997* provides four concessions to eliminate, reduce and/or provide a rollover for a capital gain made on a CGT asset used in a small business:

- the “15-year exemption”;
- the “50% reduction”;
- the “retirement exemption”; and
- the “roll-over” concession.

The concessions are designed to assist owners of small businesses by providing relief from CGT on assets related to their business which helps them to re-invest and grow, as well as contribute to their retirement savings through the sale of the business.

However, some taxpayers can access these concessions for assets unrelated to their small business, eg through arranging their affairs so that their ownership interests in larger businesses do not count towards the tests for determining eligibility for the concessions.

The amendments to avoid this are proposed to start on 1 July 2017. The small business CGT concessions will continue to be available to small business taxpayers with aggregated turnover of less than \$2 million or business assets less than \$6 million.

GST

GST treatment of digital currency

The Government will align the GST treatment of digital currency with money.

The treatment of digital (or crypto) currency for GST purposes has been hugely challenging for the Government. Digital currency refers to things such as bitcoin, although there are apparently over 600 other currencies available. ATO rulings released in December 2014 set out the ATO view that bitcoin is neither money nor a foreign currency and the supply of bitcoin is not a financial supply for GST purposes. In its view, transacting with bitcoin is akin to a barter arrangement, with similar GST consequences.

The result is that trading with bitcoin can give rise to a form of double taxation for GST purpose – once on the purchase of the digital currency and again on its use in exchange for other goods and services subject to GST.

There have been three significant developments up to this point which deal with the treatment of digital currencies:

- a Senate Economic References Committee report in 2015;
- the Government’s “Backing Australian FinTech” statement in March 2016; and
- a Government discussion paper in May 2016.

Presumably the proposed changes are a result of these developments. The changes will be designed to ensure that purchases of digital currency are not subject to GST. The Budget papers do not give specific details about how this will be achieved

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The measure will come into effect from 1 July 2017. It will have “a small but unquantifiable decrease in GST collections”. In other words, less GST will be collected – but not much.

New residential premises: purchasers to pay GST

Purchasers of newly constructed residential properties (or new subdivisions) will be required to remit the GST directly to the ATO as part of settlement.

Currently, GST is included in the purchase price and it is the developer who remits any GST. However, some developers are failing to remit the GST (despite having claimed GST credits on their construction costs).

The Budget Papers state that, as most purchasers use conveyancing services to complete their purchase, they should experience minimal impact from these changes. No mention is made of the additional administrative cost to the conveyancers or indeed the purchasers.

The measure is proposed to start on 1 July 2018.

Interestingly, the net impact of this measure appears quite significant. It is estimated to increase GST revenue by \$660 million and associated payments to the States and Territories, net of administrative costs, by \$1.6 billion over the four-year forward estimates period. The difference is due to the timing of when GST is collected and recognised.

HOUSING AFFORDABILITY

Overview

The 2017–2018 Budget contained a number of measures designed to improve Australians’ access to secure and affordable housing across the housing spectrum. These include:

- strengthening the CGT rules to reduce the risk that foreign investors avoid paying CGT in Australia;
- introducing a 50% cap on pre-approved foreign ownership in new developments;
- applying an annual charge to foreign owners who leave residential property unoccupied or not available for rent for six months or more each year;
- easing restrictions that are contributing to the supply of housing falling behind population growth and encouraging a more responsive housing market;
- improving outcomes in social housing and homelessness;
- assisting first home buyers to build a deposit inside superannuation; and
- allowing older Australians to contribute downsizing proceeds into superannuation.

Increased CGT discount for investments in affordable housing

From 1 January 2018 the CGT discount for individuals will be increased from 50% to 60% for gains relating to investments in qualifying affordable housing.

To qualify for the higher discount, housing must be provided to low to moderate income tenants, with rent charged at a discount to the private rental market rate. Tenant eligibility will be based on household income thresholds and household composition.

The affordable housing must be managed through a registered community housing provider and the investment held for a minimum period of 3 years. Any period before the time a property was purchased when it was used for affordable housing purposes will count towards the buyer’s qualifying investment period (provided the previous owner did not claim the additional discount).

The additional discount will be pro-rated for periods where the property is not used for affordable housing purposes.

The higher discount will flow through to resident individuals investing in qualifying affordable housing through a managed investment trusts.

The increased discount is not limited to investments in new affordable housing. This means that investors who elect to supply their existing properties for affordable housing will qualify for the additional discount provided the investment meets the eligibility requirements.

The Government will consult further on the implementation of this policy, including on the precise definition of affordable housing and tenant eligibility, and what qualifies as rent charged below the market rate.

SUPERANNUATION

No major new super measures, but 1 July reforms loom large

The Government did not announce any new major superannuation measures in the Budget. This will be a welcome relief for the super industry, which already has enough on its plate with major reforms set to start on 1 July 2017. As is the case with any large-scale changes such as the 1 July 2017 super reforms, refinements are often necessary to address unanticipated consequences as part the implementation process.

Super changes announced

A range of superannuation measures were announced in the Budget, including:

- the current tax relief for merging superannuation funds will be extended until 1 July 2020;

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- the non-arm's length income provisions will be amended from 1 July 2018 to reduce opportunities for members to use related-party transactions on non-commercial terms;
- limited recourse borrowing arrangements will be included in a member's total super balance and the \$1.6 million pension transfer balance cap from 1 July 2017;
- a person aged 65 or over to make a non-concessional contribution of up to \$300,000 from the proceeds of selling their home from 1 July 2018; and
- a first home super saver scheme will allow future voluntary contributions to superannuation to be made by first home buyers from 1 July 2017 to be withdrawn for a first home deposit, along with associated deemed earnings.

Merging super funds: tax relief extended until 1 July 2020

The Government will extend the current tax relief for merging superannuation funds until 1 July 2020 to remove tax as an impediment to fund mergers and industry consolidation.

Since December 2008, tax relief has been available for APRA regulated superannuation funds under Div 311 of the ITAA 1997 to transfer capital and revenue losses to a new merged fund, and to defer taxation consequences on gains and losses from revenue and capital assets. This tax relief was due to lapse on 1 July 2017. It will now be extended until 1 July 2020.

The Government said that this tax relief for merging funds will be temporarily extended as the Productivity Commission completes a review into the efficiency and competitiveness of the super industry. According to the Government, extending this relief will ensure super fund members' balances are not reduced by tax when superannuation funds merge.

Merger tax relief will apply until 1 July 2020.

Note that the Government also released exposure draft legislation on 13 April 2017 proposing to expand the tax relief available to superannuation funds when mandatorily transferring assets as part of the transition to the MySuper rules (generally by 1 July 2017).

Super fund related-party transactions: non-arm's length income rules to be amended

The non-arm's length income (NALI) provisions for super funds will be amended from 1 July 2018 to reduce any opportunities for members to use related-party transactions on non-commercial terms to increase superannuation savings.

Specifically, the NALI provisions in s 295-550 of the *Income Tax Assessment Act 1997* will be amended to ensure expenses that would normally apply in a commercial transaction are included when considering

whether the transaction is on a commercial basis. A super fund's non-arm's length income (also known as "special income") is taxed at 47% instead of the 15% concessional rate.

The measure will seek to ensure that the super reform legislation operates as intended. Essentially, it appears to be aimed at preventing individuals from using non-arm's length arrangements with their superannuation fund to circumvent the pension balance cap and total superannuation balance threshold.

Super borrowings: LRBA integrity measure for pension cap

As an integrity measure, the use of limited recourse borrowing arrangements (LRBAs) by superannuation will be included in a member's total superannuation balance and for the purposes of the \$1.6 million pension transfer balance cap from 1 July 2017.

According to the Government, LRBAs can potentially be used to circumvent contribution caps and effectively transfer growth in assets from the accumulation phase to the retirement phase that is not captured by the pension transfer balance cap. From 1 July 2017, the outstanding balance of an LRBA will be included in a member's annual total superannuation balance. In addition, the repayment of the principal and interest of an LRBA from a member's accumulation account will be a credit in the member's pension transfer balance account. The measure is expected to save only \$4 million over the forward estimates.

The Government previously released exposure draft legislation on 27 April 2017 proposing to include the use of LRBAs by self managed super funds in a member's total superannuation balance and the \$1.6 million pension transfer balance cap. Importantly, that draft legislation only proposed to apply on prospective basis in relation to borrowings that are entered into on or after the commencement of the Bill. So the Budget proposal to apply such an integrity measures to outstanding LRBA balances from 1 July 2017 seems a significant shift in policy.

Super contributions of proceeds up to \$300,000 from downsizing a home

The Government will allow a person aged 65 or over to make a non-concessional contribution of up to \$300,000 from the proceeds of selling their home from 1 July 2018. These contributions will be in addition to those currently permitted under existing rules and caps and they will be exempt from the existing age test, work test and the \$1.6 million total superannuation balance test for making non-concessional contributions (which applies from 1 July 2017).

The measure will apply to sales of a principal residence owned for the past 10 years or more. Both members of a couple will be able to take advantage of this measure for the same home. The measure seeks to reduce a barrier to downsizing for older people to enable more effective use of the housing stock by freeing up larger homes.

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Note that the proceeds from downsizing a home in this manner are not proposed to be exempt from the Age Pension assets test.

First home super saver scheme

The Government will encourage home ownership by allowing future voluntary contributions to superannuation made by first home buyers from 1 July 2017 to be withdrawn for a first home deposit, along with associated deemed earnings.

Concessional contributions and earnings that are withdrawn will be taxed at marginal rates less a 30% offset. Combined with the existing concessional tax treatment of contributions and earnings, this will provide an incentive that will enable first home buyers to build savings more quickly for a home deposit.

Under the measure up to \$15,000 per year and \$30,000 in total can be contributed, within existing caps. Contributions can be made from 1 July 2017. Withdrawals will be allowed from 1 July 2018 onwards. Both members of a couple can take advantage of this measure and combine savings for a single deposit to buy their first home together.

This measure is expected to have a cost to revenue of \$250 million over the forward estimates. The ATO will be provided with \$9.4 million to implement the measure.

A previous scheme, the First Home Saver Accounts (FHSA) scheme, was abolished from 1 July 2015, although people still have until 30 June 2017 to make claims for government contributions. The scheme operated on the basis that people made contributions to a FHSA which then resulted in a government contribution, the amount of which depended on how much the individual's personal contribution was. To claim a government contribution, the person must have been a resident of Australia for tax purposes.

The main features of that FHSA were as follows:

- The government made a 17% contribution on the first \$6,000 a person deposited each financial year. For example, a personal contribution of \$1,000 would result in a government contribution of \$170.
- The interest a person earned on their account was only taxed at a rate of 15%.
- The person had to save at least \$1,000 each year over at least four financial years before they could withdraw the money. The four years did not have to be consecutive.
- The maximum account balance was capped at \$90,000. After savings reached this level, only interest and earnings could be added to the balance.

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