Retirewell eNewsletter

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# Hockey sticks it to almost everyone in ‘cut and build’ Budget we had to have

In every decade, there is usually at least one Federal Budget that ends up being a game-changer in Australia. The Budgets of 1988 (return to surplus), 1996 (spending reductions), 2000 (introduction of GST) and 2006 (super reform) were strategies that permanently altered the economic dynamics of the Australian economy.

The 2014 Budget delivered earlier this month by the Treasurer, Mr Joe Hockey, is likely to join this list, as it facilitates the move to smaller government, more infrastructure investment and less household dependency on government payments.

Without the Budget cuts and controls on spending growth, the end result would have been ongoing deficits and growing government debt, reaching $667 billion in 2023-24 according to Treasury estimates.

The Budget deficit will fall from its current $49.9 billion to $29.8 billion next financial year. By 2017-18, it should be reduced to $2.8 billion.

The Budget savings are modest in the next few years (with the Government having been restrained by the soft economy which is expected to grow below trend over the next two years, as well as by its first-term promises which pushed a lot of the changes back until after the next election).

The so-called cuts to education and health from 2017-18 are really only reductions to the previous Labor Government’s promised but unfunded boost to spending in these areas. Commonwealth funding of government schools in 2018 will still be 36% higher in real terms than this year, while Commonwealth spending on hospitals will be 15% higher in real terms than last year.

Nevertheless, by 2023-24, if fully implemented, the measures would produce net savings of $271 billion, which means that the our gross debt is likely to peak at $389 billion, or 19% of gross domestic product (GDP), which is considerably less than the 73% global average.

So much for cutting, what about building? The Government said it would provide an extra $11.6 billion to establish an Infrastructure Growth Package to boost total infrastructure investment by federal, state and local governments, as well as the private sector (mainly in major roads and a second Sydney airport) to more than $125 billion by 2019-20. This will result in annual economic growth being boosted by 1%, according to Treasury estimates.

Treasury expects economic growth to slow from 2.75% to 2.5% next financial year before recovering to 3% in 2015-16. Inflation is forecast to fall from 3.25% to 2.25% next financial year before edging up to 2.5% in 2015-16. Unemployment is expected to increase from 6% to 6.25% next financial year with it staying steady in 2015-16.

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# TAXATION

## TEMPORARY DEFICIT LEVY ON HIGH INCOME EARNERS

**From 1 July, 2014**, the Government will impose a 2% Temporary Budget Repair Levy on high income earners for the next three financial years. This means that the top marginal tax rate of 45% (which applies to that portion of taxable income over $180,000) will effectively be 47% for the three financial years during which the levy applies. When the 2% basic Medicare levy is added (as from 1 July this goes up from 1.5% to help pay for the National Disability Insurance Scheme), the effective top marginal tax rate will be 49% for the three levy years.

This increase will also apply to the non-complying superannuation funds and to the non-arm's length income of a complying superannuation fund. Any non-TFN contributions income of a superannuation fund will also be subject to tax at 47% (rather than 45%).

The effect of the levy can be reduced by a high income earner increasing his or her concessional superannuation contributions to $35,000 (for those aged 50 or more at any time during the 2014-15 financial year) and $30,000 (for other super fund members). The effect of the levy also can be reduced by substituting fringe benefits for assessable salary until 31 March, 2015 as the fringe benefits tax rate will increase to 49% only for two FBT years from 1 April, 2015 to 31 March, 2017.

*COMMENT: Draft legislation has already been released to implement the levy and the years to which the levy applies are explicitly set out. Nevertheless, hopefully the levy will in fact only be temporary, and not temporary in the historical sense of the word: that is indefinitely.*

*When Pitt the Younger introduced income tax to England in the 1799 Budget it was supposed to be only a temporary measure to finance the war against the French.*

*Income tax was in fact abolished in 1802, but reintroduced in 1803 when hostilities with the French recommenced. It was again abolished in 1816 after the final defeat of Napoleon 1. Income tax was again re-introduced in 1842 as a means of financing the English national debt and is still with us. Curiously, income tax was re-introduced by Sir Robert Pell after winning the 1841 general election during which he had opposed a tax on income. Some things never change.*

## FBT INCREASED TO PREVENT BUDGET REPAIR LEVY AVOIDANCE

The 2% levy will also be reflected in other tax rates based on calculations that include the top marginal tax rate such as Fringe Benefits Tax (FBT). The FBT rate will increase from 47% to 49% **from 1 April, 2015** until 31 March, 2017.

The existing value of benefits received by employees of Public Benevolent Institutions (PBIs) and other recognised organizations will be protected by an increase in the annual FBT caps which will be aligned with the FBT rate from 1 July 2015.

The PBI and other recognised organizations grossed-up annual cap increases to $31,177 per employee (currently $30,000), while the public hospitals and ambulances service grossed-up annual cap will increase to $17,667 per employee (currently $17,000).

## FUEL EXCISE INDEXATION TO BE RESUMED

**From 1 August, 2014,** the excise on fuel (other than aviation fuel) will start to be indexed again every six months after having been frozen for 13 years. This will raise the price of petrol by 1c a litre every year and will increase the average motorist's fuel bill by 50c a week.

## CO-PAYMENT FOR MEDICAL SERVICES TO BE INTRODUCED

**From 1 July, 2015**, a patient contribution of $7 will be introduced for standard GP consultations and out-of-hospital pathology and diagnostic imaging services.

Of this amount, $5 will be paid into a new Medical Research Future Fund, which is expected to be worth $20 billion by 2020, and be making annual grants of $1 billion.

Concession card holders and children under the age of 16 will only need to make this co-payment for the first 10 visits in a year – a total of up to $70 a year.

Patients who are not bulk-billed will have their Medicare refund reduced by $5.

The Government also has proposed a $5 increase to $42.70 for pharmaceuticals on PBS, with concession card holders paying an additional 80c to bring the cost to $6.90 a script.

The safety net threshold will increase **from 1 January, 2015** for four years by 10% a year and the concessional safety net by two prescriptions a year.

## TAX OFFSETS ABOLISHED

The Mature Age Worker Tax Offset (MAWTO) will be abolished from 1 July, 2014. It will be replaced with a new incentive payment called Restart, comprised of payments up to $10,000 over two years to employers who hire mature aged job seekers, aged 50 or over, who have been receiving income support for at least six months.

The Dependent Spouse Tax Offset, currently available for taxpayers with a dependent spouse born before 1 July, 1952, will be abolished for all taxpayers from 1 July, 2014.

## COMPANY TAX TO BE CUT

**From 1 July, 2015,** the company tax rate will be cut from 30% to 28.5% and this will reduce franking credits accordingly.

For 3,000 large companies with revenue of more than $5 million per annum, the 1.5% reduction will be offset by the 1.5% paid parental scheme levy.

For the 800,000 small companies not required to pay the levy, this will mean higher net profits which should lead to higher dividends, in order to make up for the loss of franking credits.

## HIGHER EDUCATION COSTS TO INCREASE

The income threshold for repayment of Higher Education Loan Program (HELP) debts will reduce **from 1 July, 2016** and the indexation of HELP debts will be adjusted **from 1 June, 2016**.

A new minimum threshold, set at 90% of the minimum threshold that would have otherwise applied in 2016-17 (estimated to be $50,638) will apply for the repayment of HELP debts.

A 2% per annum repayment rate will apply to debtors with incomes above the new minimum threshold, instead of the current 4% per annum.

The annual indexation applied to HELP debts will be adjusted from the Consumer Price Index to a rate equivalent to the yields on 10 year bonds issued by the Australian Government, capped at 6% per annum. Furthermore, **from January, 2016**, universities, private colleges and TAFEs – will be able to set their own course fees.

The Government will mandate that 20% of the additional revenue raised from higher fees be used to fund Commonwealth scholarships to support disadvantaged students.

Students who are studying, or who have now accepted and deferred a course offer, will continue to be charged current fee levels, as long as they have completed their course by December, 2020.

### RISE IN MEDICARE LEVY THRESHOLD

**From 1 July, 2013**, the Medicare levy low-income threshold will increase to $34,367 for couples and the additional amount of threshold for each dependent child or student will be increased to $3,156. The thresholds for individuals and pensioners will stay the same at $20,542 and $32,279 respectively.

### PAUSE TO INDEXATION OF SURCHARGE AND REBATE

Indexation of the income thresholds for the Medicare Levy Surcharge and Private Health Insurance Rebate will be paused for three years **from 1 July, 2015**.

### FIRST HOME SAVER ACCOUNTS AXED

This scheme, which started in October 2008, will be abolished, as the take-up rates have been low. New accounts opened on or after Budget night will not be entitled to any Government co-contribution. For existing accounts, the Government co-contributions will cease **from 1 July, 2014**.

Any tax and Centrelink concessions associated with new or existing accounts will cease from 1 July, 2015. Account holders will be able to access their account balance without restriction from that date.

As at December, 2013, there were only 46,000 accounts open with an average account balance of $11,337.

# SUPERANNUATION

### SUPER GUARANTEE RATE TO BE PAUSED FOR THREE YEARS AT 9.5%

The Budget proposes to increase the super guarantee (SG) rate from 9.25% to 9.5% for **2014-15** and the 9.5% rate will apply for the following three years. With effect **from 1 July, 2018,** the SG rate will increase to 10% and a further 0.5% each year until the rate reaches 12% in respect of the 2022-23 financial year.

The now proposed, as against the previously legislated, rates are set out in the following table:

| Financial Year | Budget 2014 | Previously (as legislated) |
|---|---|---|
| 2014/15 | 9.5% | 9.5% |
| 2015/16 | 9.5% | 10% |
| 2016/17 | 9.5% | 10.5% |
| 2017/18 | 9.5% | 11% |
| 2018/19 | 10% | 11.5% |
| 2019/20 | 10.5% | 12% |
| 2020/21 | 11% | 12% |
| 2021/22 | 11.5% | 12% |
| 2022/23 | 12% | 12% |

### EXCESS NON-CONCESSIONAL CONTRIBUTIONS TAX RELIEF

Following the resolution in last year's Budget of the problem of unfair tax on excess concessional contributions, the Government has now solved the same problem regarding excess non-concessional contributions.

Excess non-concessional contributions arising in respect of **2013-14** and subsequent financial years will, at the election of the super fund member, be returned to the member together with accrued earnings. The accrued earnings will be included in the member's income and taxed at marginal rates.

However, the returned excess contribution will not be taxed when repaid (as the member received no tax benefit in making the contributions in the first place).

If the member does not elect to have the excess contributions returned, he or she will be subject to excess non-concessional contributions tax at (currently) 46.5% which will increase to 49% for the next three years, before reducing to 47%.

### IMPROVEMENTS TO INDEXATION OF DEFENCE FORCE SUPER BENEFITS

Not before time, improvements will be made to the indexation of payments made under the Defence Force Retirement Benefits (DFRB) and Defence Force Retirement and Death Benefits (DFRDB) superannuation schemes.

**From 1 July, 2014**, DFRB and DFRDB superannuation scheme members aged 55 and over will have their superannuation benefits indexed by the better of the Consumer Price Index and the Pensioner and Beneficiary Living Cost Index, with reference also to a benchmark level of male total average weekly earnings.

## SOCIAL SECURITY

### AGE PENSION AGE TO BE INCREASED AGAIN

The Budget proposal is to ultimately increase the qualifying age for the age pension to 70. This qualifying age will apply to anyone **born on or after 1 January, 1966**.

Currently the qualifying age is in the process of being gradually increased from 65 to 67. This affects those currently under age 62 (whose pension age will be 65.5), those under 60.5 (whose pension age will be 66), those under 59 (whose pension age will be 66.5) and those under 57.5 (whose pension age will be 67).

The increase in qualifying age from 67 will affect anyone born after 1 July 1958 (i.e. under 56) and will be completely implemented for anyone born after 1 January 1966. So anyone under 48.5 will have an age pension age of 70.

| People born between | Eligibility age |
|---|---|
| Before 1 July 1952 | 60 |
| 1 July 1952 and 31 December 1953 | 65.5 |
| 1 January 1954 and 30 June 1955 | 66 |
| 1 July 1955 and 31 December 1956 | 66.5 |
| 1 January 1957 and 30 June 1958 | 67 |
| 1 July 1958 and 31 December 1959 | 67.5* |
| 1 January 1960 and 30 June 1961 | 68* |
| 1 July 1961 and 31 December 1962 | 68.5* |
| 1 January 1963 and 30 June 1964 | 69* |
| 1 July 1964 and 31 December 1965 | 69.5* |
| 1 January 1966 and later | 70* |

* Changes proposed in this Budget

Given increased longevity and improved health standards, one can see the logic behind increasing the qualifying age for the age pension. When the age pension was introduced in 1909 the male life expectancy at birth was 55, which was 10 years **below** the age pension age. The aim was to help people who lived longer than the average. A male born today has a life expectancy of just under 80 years which is 15 years **over** age pension age.

Between 2010 and 2050, the number of people aged 65 to 84 is expected to double and the number of people 85 and older is expected to quadruple. If current policies are maintained, spending on the Age Pension is projected to increase by 70 per cent over the next decade.

Importantly, this change does not mean that people will need to work to age 70, just that they will have to rely on superannuation and other savings between retiring from the workforce and reaching age 70. Currently, the super preservation age is 55, but it will be gradually increased to 60 over the next 10 years, after which super can be accessed through a transition to retirement pension even before age 65.

Those aged 48.5 or younger who will have to wait until 70 to qualify for the age pension will need to save an extra $96,432 (individual) or $145,378 (couple) to replace the foregone age pension for the five year gap.

## DEEMING THRESHOLDS LOWERED

**From 1 September, 2017**, the income test for qualification for the age pension will be made more stringent by reducing the deeming thresholds from the current $46,600 to $30,000 (single threshold) and from the current $77,400 to $50,000 (couple threshold).

The deeming thresholds apply to financial assets and attribute a notional income return from those assets for the purposes of the income test of the age pension.  The deemed income rates are currently 2% which applies to the total value of assets (that are subject to deeming) below the threshold and 3.5% on the excess above the threshold.

By lowering the deeming threshold, more income will be treated as being earned from the assets and used in applying the income test. This means an individual with deemed financial assets of $250,000 will lose $124 a year, and a couple will lose $206 a year. This effect will be magnified when deeming rates rise, as they inevitably will in the future.

It is worth remembering that the original purpose of the lower threshold was to allow pensioners to keep a few months spending money in a lower interest call account. From this perspective the new thresholds are still generous.

## INDEXATION OF PENSIONS TO BE REDUCED

The Budget proposal is to index the Centrelink age pension, disability support pension, carer payment and the Veterans Affairs service pension by reference to the Consumer Price Index (CPI), **from 1 September, 2017**. This measure applies **from 1 July, 2014** for the parenting payment

Currently, these pensions and payments are increased by reference to whichever of the following indices produces the most favourable outcome: Consumer Price Index, Male Total Average Weekly Earnings and the Pensioner and Beneficiary Living Cost Index.

While this change will not reduce these benefits, it will have the effect that these pensions and payments will not increase as fast as would have been the case if the current indexation arrangements were to continue.

This seems to be a small change, but will result in a significant reduction in the present value of pension entitlements. Based on the assumption that average weekly earnings are growing at 4% per annum and inflation at 2.5% per annum, and a couple's full age pension is now $33,000 a year, then in 10 years time at 4% per annum, the pension would have risen to $48,800 a year – at 2.5% per annum this would be $42,200 a year. In 20 years time at 4% per annum, the pension would be $72,300, but at 2.5% per annum, it would be just $54,000 a year. It is not going to make much difference in the short term, but the difference will be very noticeable in the long-term.

## PAUSE FOR INCOME AND ASSETS TEST FREE THRESHOLDS

The income and assets test free thresholds (i.e. income and assets which can be held without triggering a reduction in the age pension, disability support pension, carer payment and Veterans Affairs service pension) will be paused for 3 years **from 1 July, 2017**. This pause also will apply to Newstart Allowance, Parenting Payments and Youth Allowance for three years **from 1 July, 2014**.

## SENIORS HEALTH CARD INCOME TEST TO INCLUDE SUPER PENSION INCOME

It is proposed that **from 1 January, 2015**, income from account-based pensions will be counted under the deeming rules when determining the eligibility for the Commonwealth Seniors Health Card (CSHC). This treatment is far less generous than current treatment. The assessment of superannuation pension income will be the same for age pension recipients from 1 January, 2015. **However, all superannuation account income streams held by existing Seniors Health Card holders before 1 January 2015 will be grandfathered under the existing rules.**

**Any person with money in a superannuation accumulation account who is of age pension age before 1 January, 2015 and who wishes to maximise their current or future entitlement to the age pension and/or qualify for the Seniors Health Card should consider commencing an account-based pension before 1 January, 2015.**

Also, the Government has introduced legislation to index (based upon CPI) the current income limits applying to the eligibility for the Seniors Health Card, which are $50,000 per annum for an individual and $80,000 per annum for a couple. This will apply **from 20 September, 2014**. This is good news, since the limits have not been increased for a long time.

## CESSATION OF SENIORS SUPPLEMENT FOR SELF-FUNDED RETIREES

**From 20 September, 2014**, Seniors Health Card holders who are effectively self-funded retirees no longer will qualify for the Seniors Supplement of $876.30 per annum (single) or $660.40 (each for a couple). However, they will continue to receive the Clean Energy Supplement of $361.40 per annum (single) or $273 per annum (each of a couple). Those receiving an age pension (part or full) are not affected by this change.

## COMMONWEALTH SUBSIDY OF SENIOR CONCESSIONS TO END

**From 1 July, 2014**, the Commonwealth Government's agreement with the states to fund concessions to seniors will be terminated. This raises the question as to how the states will continue to fund discounts on council land and water rates, utilities including energy and sewerage, motor vehicle registration and public transport.

## FAMILY TAX BENEFIT PART B CAP LOWERED

**From 1 July, 2015**, the primary earner income limit for Family Tax Benefit Part B will be reduced from $150,000 per annum to $100,000 per annum and the benefit will only be available when children are less than six years old.

As an example of the impact of this on a family budget, we will take a married couple with three children aged 10, 8 and 6, where the husband earns $120,000 per annum and the wife $12,000 from part-time work. They will be worse off by $2,657 per annum.

All eligibility thresholds for Family Tax Benefit also will be paused for three years **from 1 July 2014.**

## PAID PARENTAL LEAVE SCHEME CAP REDUCED

The maximum payment from the proposed paid parental leave scheme **from 1 July, 2015** (under which 50% of the mother's salary for 26 weeks would be reimbursed) will be reduced from $75,000 to $50,000 plus super.

The current government scheme pays a maximum of $622.10 a week ($11,198 over 18 weeks).

**Of course, all the above measures are subject to the relevant legislation being passed by Parliament.**

If you have any queries or concerns regarding your financial situation, please contact your Retirewell Adviser.

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