A Clear Direction Financial Planning

Level 19, 10 Eagle Street, Brisbane QLD 4000
scottk@acleardirection.com.au
(07) 3379 6068
ABN: 85 147 572 870

2013 Budget - Personal Finance Summary

This election year budget has provided minimal substantive changes in terms of new financial planning strategies apart from restating initiatives that had already been announced. Some of the announced initiatives may provide opportunities or the need for changes to structuring of assets. However we need to keep in mind that the implementation of any proposed changes may be dependant on the result of this year's federal election.

This summary will look at the following major changes grouped into three main areas – retirement planning, tax planning and government benefit planning:

Retirement Planning

- Increase in the concessional contributions cap from $25,000 to $35,000 for individuals aged 60 and over from 1 July 2013
- Increase in the concessional contributions cap from $25,000 to $35,000 for individuals aged 50 and over from 1 July 2014
- The first $100,000 of retirement phase superannuation earnings to remain tax free with any excess taxed at 15% from the 1 July 2014
- Minimum payment amounts for account based pensions to revert to original settings
- Deeming rules for account based pension income
- Superannuation guarantee rate to progressively rise from 9% to 12%
- Removal of the maximum age limit of superannuation guarantee contributions from 1 July 2013
- Excess contributions to be taxed at marginal tax rates rather than at the highest marginal tax rate
- Ability to withdraw excess contributions
- Concessional tax treatment for deferred lifetime annuities equivalent to those applied to superannuation assets supporting income streams
- Pilot program to assist age pensioners to downsize their family home

Tax Planning

- Increased Medicare levy from 1 July 2014
- Increasing the Medicare Levy low income thresholds
- Deferral of 2015/16 income tax cuts
- Net medical expenses tax offset (NMETO) to be phased out
- Work related self education tax deductible expenses to be capped at $2,000 from 1 July 2014

Government Benefit Planning

- Replacement of the baby bonus with family payment arrangements
- Discounts applying to up-front and voluntary payments under the Higher Education Loan Program (HELP) will be removed from 1 January 2014
- Increase to the income free area for Newstart allowances
- Access to government benefits whilst overseas – temporary absence reduced from 3 years to 1 year
- Family Tax Benefit Part A proposed increases deferred

Each of the above items has been addressed in a little more detail in the following sections.

Increase in concessional contributions cap for individuals aged 60 and over from 1 July 2013

A $35,000 concessional contributions cap will be provided for all people aged 60 and over from 1 July 2013.

Strategy Thoughts

If you are already 60 or turning 60 next financial year, consideration should be had of whether it makes sense to increase the level of concessional contributions being paid into super. If there is a tax benefit to be gained considerations should be given as to how to best afford the extra concessional contributions either through reducing the level of savings held external to the superannuation system or drawing an increased level of pension from an account based pension.

Increase in concessional contributions cap for individuals aged 50 and over from 1 July 2014

A $35,000 concessional contributions cap will be provided for all people aged 50 and over from 1 July 2014.

Strategy Thoughts

If you will be aged 50 or above after the 1st of July 2014, consideration should be had of whether it makes sense to increase the level of concessional contributions being paid into super. If there is a tax benefit to be gained you could start planning on how to fund the increased level of concessional contribution through starting to save now.

The first $100,000 of retirement phase superannuation earnings to remain tax free with any excess taxed at 15% from 1 July 2014

The tax exemption for earnings on superannuation assets supporting income streams will be limited to the first $100,000 of annual earnings for each individual and taxing earnings above that threshold at the concessional rate of 15 per cent from 1 July 2014. Equivalent arrangements will be enacted for defined benefit schemes.

Under this measure, the $100,000 threshold will be indexed to the Consumer Price Index and will increase in $10,000 increments. For assets that were purchased before 5 April 2013, the measure will only apply to capital gains that accrue after 1 July 2024. Capital gains that are subject to the tax will receive a 33 per cent discount, and will therefore be effectively taxed at a rate of 10 per cent.

Annual earnings relates to the income generated by assets, including realised capital gains, and is not in relation to the amounts withdrawn from superannuation pension accounts.

Strategy Thoughts

If this change is enacted and it is likely that you will exceed the $100,000 annual income limit whilst in account based pension phase, consideration should be given to the structuring of assets either through evening up the account balances of each member of a couple and/or considering whether assets can be held directly in your own name and not see you pay any tax on income in accordance with the Senior Australian Tax Offset.

Another possible consideration would be to look to manage the capital gains basis of an account to minimize the impact of realized capital gains either to the member or to future beneficiaries of the proceeds from the account on death.

Before making any changes consideration will need to be had of each couple or individual's situation. This will be a point of discussion with clients once there is greater certainty that the proposed initiative is going to be implemented.

[Return to Page 1]

Minimum payment amounts for account based pensions

This issue was not included in the budget papers suggesting that payment amounts will revert to the original minimum levels. This will see the minimum drawdowns for account based pensions (as a percentage of the account balance at the 1st of July or commencement of the pension):

Age of Beneficiary	2012-13 % factor
Under 65	4.00
65 - 74	5.00
75 - 79	6.00
80 - 84	7.00
85 - 89	9.00
90 - 94	11.00
95 or over	14.00

Term Allocated Pension (TAP) payment factors will also return to original levels with the exact details dependant on the individual arrangements for an account.

Strategy Thoughts

Account based pension holders who have not yet turned 60 and are continuing to work (Transition to Retirement pension accounts) will need to consider whether it remains in their interests to keep the transition to retirement pension in place. In the vast majority of cases it will still make sense.

If account holders are forced to draw out more than required consideration will need to be had as to where to invest those excess to requirement withdrawals.

Deeming rules for account based pension income

Normal pension income test deeming arrangements will be extended to superannuation account-based income streams assessed from 1 January 2015. Products held by pensioners before 1 January will be grandfathered.

This means that rather the level of deemed income from income stream pension payments being calculated based on the level of payment drawn with an amount deducted in relation to the life expectancy of the account holder or primary beneficiary, the government will calculate a level of deemed income based on the asset value of the account.

This is likely to see account holders deemed to be earning a much greater level of income for means testing of government benefits purposes (e.g. Age Pension & Disability Support Pension)

Strategy Thoughts

If this proposed change is implemented, those already holding superannuation account based income stream accounts who are already receiving or likely to receive means tested government benefits will need to carefully consider the implications of restructuring an account based pension. Currently many holders of these accounts will add new contributions each year or roll over to another provider. This would be deemed to be the commencement of a new account based pension and as such would fall under the new regime through adding extra contributions or moving to an alternative provider if implemented after 1 January 2015.

[Return to Page 1]

Superannuation guarantee rate to progressively rise from 9% to 12%

The superannuation guarantee rate will progressively increase from 9 to 12 per cent, from 1 July 2013 to 1 July 2019.

Strategy Thoughts

Consideration of these increased rates will need to be had for those who are already looking to maximise their level of concessional contributions each year to ensure that excess contributions are not made.

Regular investment strategies may need to be amended to take account of the extra level of contribution.

Removal of the maximum age limit of superannuation guarantee contributions from 1 July 2013

The maximum age limit for the superannuation guarantee will be abolished, to increase incentives for workers aged 70 and over to remain in the workforce and further boost retirement savings.

Strategy Thoughts

There is now another small incentive for those who want to keep working past age 70.

Excess contributions to be taxed at marginal tax rates rather than at the highest marginal tax rate

From 1 July 2013 the excess contributions tax system will be made fairer by taxing excess concessional contributions at a person's marginal tax rate, plus an interest charge, rather than always taxing them at the top marginal tax rate.

Strategy Thoughts

This and the next proposed change regarding the ability to withdraw excess contributions will provide a buffer against paying extra tax. It will allow greater comfort in maximizing the concessional contribution limit each year knowing that if excess contributions are made this can be rectified.

Depending on the level of interest charge applied by the Australian Tax Office and how this is applied, it may actually encourage directing extra regular contributions into super from each pay packet in order to get those assets into the more friendly tax environment for investment earnings.

Ability to withdraw excess contributions

Individuals will also be given greater choice by allowing them to withdraw any excess concessional contributions from their super fund.

Concessional tax treatment for deferred lifetime annuities equivalent to those applied to superannuation assets supporting income streams

The government has sought to encourage the take-up of deferred lifetime annuities by providing them with the same concessional tax treatment that earnings on superannuation assets supporting retirement income streams receive from 1 July 2014.

Strategy Thoughts

This firm has not looked to recommend the use of such products due to a belief that a better outcome can be achieved through the careful management of a portfolio of assets. This introduction of this change will lead to a re-assessment of the use of such products with future analysis to be made available to clients in due course.

[Return to Page 1]

Pilot program to assist age pensioners to downsize their family home

The Government will trial a new measure to assist senior Australians to downsize their home without putting their eligibility for the Age Pension at risk. A three year trial will commence on 1 July 2014 where senior Australian homeowners who downsize when buying another home will have an option to invest at least 80 per cent of surplus funds remaining (up to a cap of $200,000) in a special account. The funds invested in the account would be exempt from the Age Pension means test for up to 10 years. The scheme would only be available to Australians over Age Pension age who have owned their home for at least 25 years.

Strategy Thoughts

Care around the decision to downsize should first be based on the potential cost to implement, some suggesting it costs up to 8% of the value of the new property.

That said the above proposal would provide significant Age Pension benefits for those where it makes personal and financial sense to downsize.

Increased Medicare Levy from 1 July 2014

From 1 July 2014 the Government will increase the Medicare levy by half a percentage point from 1.5 to 2 per cent of taxable income, to provide a funding source for DisabilityCare Australia.

Strategy Thoughts

This places a small extra incentive to salary sacrifice income into super where possible, as the tax benefit from making salary sacrifice contributions will increase by 0.5 of a percentage point.

Increasing the Medicare Levy low income thresholds

The Government will increase the Medicare levy low income threshold to $20,542 for individuals and $33,693 for families for 2012-13. The additional amount of threshold for each dependent child or student will also increase to $3,094. The Medicare levy threshold for pensioners eligible for the Seniors and Pensioners Tax Offset will rise to $32,279.

Deferral of 2015/16 income tax cuts

The 2015-16 personal income tax cuts were designed to assist households on the expectation of an increase in the carbon price to $29 in 2015-16 from the fixed price of $25.40 in 2014-15. As the carbon price is now projected to be around $12 in 2015-16, these tax cuts will be deferred until the carbon price in the Budget is estimated to rise above $25.40. All existing household assistance will remain in place.

Net medical expenses tax offset (NMETO) to be phased out

The net medical expenses tax offset (NME tax offset) will be phased out with transitional arrangements applying to those who currently claim the offset.

From 1 July 2013, those taxpayers who claimed the NME tax offset in the 2012/13 income year will continue to be eligible for the offset in the 2013/14 income year if they have eligible out-of-pocket medical expenses above the relevant thresholds. Similarly, those who claim the NME tax offset in the 2013/14 income year will continue to be eligible for the offset in the 2014/15 income year.

The NME tax offset will continue to be available for taxpayers for out-of-pocket medical expenses relating to disability aids, attendant care or aged care expenses until 1 July 2019 when *DisabilityCare Australia* becomes fully operational and aged care reforms have been in place for several years.

[Return to Page 1]

Work related self education tax deductible expenses to be capped at $2,000 from 1 July 2014

From 1 July 2014, the government plans to introduce a $2,000 cap on the tax deduction for work-related self-education expenses.

Strategy Thoughts

If considering work related self education this change may provide an incentive to bring forward those self education plans so that as much as possible of the cost falls before the 30 June 2014.

Replacement of the baby bonus with family payment arrangements – from 1 March 2014

From 1 March 2014 Family Tax Benefit Part A (FTB Part A) payments will be increased by $2,000, to be paid in the year following the birth or adoption of a first child or each child in multiple births, and $1,000 for second and subsequent children. The additional FTB Part A will be paid as an initial payment of $500, with the remainder to be paid in seven fortnightly installments.

Parents who take up Paid Parental Leave (PPL) will not be eligible for the additional FTB Part A component. However, the work test under the PPL scheme will be extended so that parents will be able to count periods of government PPL as —work, just like employer-funded PPL.

As a result of these reforms, the Baby Bonus will be abolished.

Discounts applying to up-front and voluntary payments under the Higher Education Loan Program (HELP) will be removed from 1 January 2014

The following discounts relating to the Higher Education Loan Program will be removed from 1 January 2014:

- The 10% discount available to students electing to pay their student contribution up-front, and
- The 5% bonus on voluntary payments made to the Tax Office of $500 or more.

Strategy Thoughts

If you were planning or able to make a voluntary payment on your HELP debt, doing so before the end the year would make sense.

Increase to the income free area for Newstart allowances from 20 March 2014

From 20 March 2014 the income free area for Newstart and other similar allowances will increase from $62 to $100 a fortnight, with indexing by CPI from 1 July 2015.

Access to government benefits whilst overseas – temporary absence reduced from 3 years to 1 year

The Government will change the allowed period of temporary absence from Australia for accessing certain family and parental payments from three years to one year from 1 July 2014. Affected payments include Family Tax Benefit Part A, Schoolkids Bonus and Paid Parental Leave.

Family Tax Benefit Part A proposed increases deferred

The Government will not proceed with the increase to FTB-A announced in the 2012-13 Budget.

[Return to Page 1]

Summary of major strategy considerations

As mentioned in the introduction, care needs to be taken in making changes to your financial planning strategy based on the measures announced in the budget due to the upcoming federal election. That said, here are some possible strategy modifications arising from this year's budget:

- Those in the workforce who will be 60 or older from 1 July 2013 should consider strategies to increase the level of concessional contributions being paid into superannuation up to the new $35,000 limit.
- Those in the workforce who will be 50 or older from 1 July 2014 should consider strategies to increase the level of concessional contributions being paid into superannuation up to the new $35,000 limit.
- Those who are or are likely to generate more than $100,000 of income (including realised capital gains) within a superannuation income stream account should start to consider possible course of action to minimise the impact of this proposed change.
- Restoration of pension payment requirements back to higher minimum withdrawals rates may require a re-assessment of the continued use of a transition to retirement pension.
- Restoration of pension payment requirements back to higher minimums withdrawal rates may require an assessment of where to invest any pension payments that are more than required.
- Those who are looking to add more to an account based pension or switch provider may want to plan for this to occur before 1 January 2015 due to the changes to means testing deeming rules.
- Those who are making the maximum allowable concessional contributions into super should consider the implications of receiving 9.5% standard employer super contributions from 1 July 2013 and adjust salary sacrifice levels accordingly.
- Salary sacrifice strategies to be re-assessed under the new Medicare Levy arrangement from 1 July 2014.
- Those turning 70 to consider the benefits of the continued superannuation guarantee contributions.
- Those looking to incur work related self education costs may look to bring forward that decision so that more of the expense falls before 1 July 2014.
- Those with a HELP debt may want to consider a voluntary repayment before 1 January 2014 in order to receive a 5% discount.

[Return to Page 1]

Concluding Comments

Overall the budget has provided a number of changes in terms of personal finance outcomes that need to be carefully considered. The major implications are for retirement planning strategies.

The further tinkering with the superannuation system whilst further undermining confidence in the system should not provide significant concerns for the vast majority of superannuation members. Those who are likely to generate more than $100,000 of income from their superannuation account will need to consider whether there are any strategies to minimise the impact of this proposed change.

A pleasing aspect is that the government has chosen not to tamper with the tax free status of draw downs from superannuation accumulation or pension accounts for those 60 years and older.

Investing through superannuation to provide for retirement therefore remains a very effective strategy with:

- Compulsory employer contributions
- Tax advantaged contributions and earnings through the accumulation stage, now at slightly higher concessional contribution rates for older superannuation account members
- Tax free superannuation withdrawals after the age of 60
- The first $100,000 of income received tax free whilst in pension phase
- Minimal rules for withdrawing superannuation

If you would like to discuss any of the details contained in the budget and how those details impact your situation please do not hesitate to be in contact.

This document has been prepared as a brief summary of the 2013 Federal Budget as it impacts on personal finances. It is a publication of A Clear Direction Financial Planning. It contains general financial information. Readers should check this information with a professional financial adviser before acting on any of the material contained in this document.

[Return to Page 1]