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Can You Plan Around the 2% Debt Tax?

The introduction of the debt tax, or the Temporary Budget Repair Levy as it is formally known, may be the only certainty in the Government's first Federal Budget delivered on 13 May.

The rest – co-payments for doctor's visits, deregulated university fees, cuts to family benefits, tightening of access to disability pensions, increasing the pension age to 70, etc. - are unlikely to see the light of day in their current form.

For those likely to be affected by the debt tax, the most common questions asked are: will the debt tax become law and will I have to pay it? The answers are probably yes and it depends.

The Labor Party has stated it will not stand in the way of the debt tax, but the Greens have come out in opposition to the tax and instead want more permanent reform "by shaving the top off the multi-billion dollar profits of big mining and banking corporations." However, with Labor's support for the tax, the legislation has a majority in both the House of Representatives and the Senate regardless of the position of the Greens.

What is the Tax and Who Will Pay It?
The debt tax will apply from 1 July 2014 until 30 June 2017. The tax is payable at a rate of 2% on every dollar of a taxpayer's annual taxable income over $180,000. In effect, the top marginal tax rate will become 49%.

Be aware that if you have a one-off spike in income after 1 July 2014, for example from the proceeds of a sale of business, the debt tax is likely to impact on this one-off increase in personal income.

Individuals with a taxable income of $180,000 or less will not pay the levy except where their income (or part thereof) is subject to some other tax rate based on the top personal marginal tax rate. For example, the debt levy will apply to the unearned income of minors once income is above $416. This is generally where income is distributed to a minor through a family trust. This is the Government's way of ensuring people cannot avoid the debt tax by simply distributing more income to their kids through a family trust.

The debt tax will also apply to non-resident taxpayers, for example where a non-resident is a beneficiary of an Australian trust.

In conjunction with the debt tax, the Fringe Benefits Tax (FBT) rate will increase to 49% to prevent anyone using the FBT system to avoid paying the tax. The FBT rate will increase from 47% to 49% from 1 April 2015 until 31 March 2017.

For employees of charities, not-for-profits and certain other entities, the exemption threshold from FBT will increase to ensure that the total value of cash benefits received by these employees are not affected.

Can You Plan Around the Debt Tax?
Yes, you can. The difference in timing between the introduction of the debt tax on 1 July 2014 and the increase to the FBT rate on 1 April 2015 means that you have nine months to utilise an effective salary sacrifice agreement and bring your taxable income below the $180,000 threshold for the year ending 30 June 2015. Plus, you have another opportunity to reduce your taxable income when the FBT rate is reduced from 1 April 2017 until the debt tax is removed on 30 June 2017. In effect, it is possible in some circumstances to utilise effective salary sacrifice agreements to reduce your taxable income below the debt tax threshold level for the 2015 and 2017 income years.

Just be aware that there are certain rules that must be followed for a salary sacrifice agreement to be effective. No doubt this will be an area that the Australian Taxation Office (Australian Taxation Office) will be looking at very closely in future years.

Talk to us today about the tax planning opportunities available to you.

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What Will Change From 1 July 2014?

Individuals

- **Temporary budget repair** Levy – adds 2% to the tax rate for every dollar of a taxpayer's annual taxable income over $180,000.
- **Increase in the Medicare levy** from 1.5% to 2%.
- **Superannuation guarantee charge increases** from 9.25% to 9.5%.
- **Aged care reforms** introduce new assets tests for resident's accommodation and care fees.

Business

- **R&D incentive reduced** – in the 2014/2015 Federal Budget, the Government announced that the Research & Development Tax Incentive will be reduced by 1.5% from 1 July 2014. This means the refundable offset will be reduced to 43.5% while the non-refundable offset will be reduced to 38.5%. While it is uncertain whether the legislation enacting this change will pass the current Parliament, businesses undertaking R&D activities this year may want to consider bringing forward expenditure to maximise their claim.
- **Living away from home allowance (LAFHA) transitional period ends** on 30 June 2014. Now, the main condition to be satisfied is that the employee must have a normal place of residence in Australia that is maintained for their "personal use and enjoyment" while they are living and working in another location. This means that the employee cannot rent out their usual residence while they are away. In most cases, LAFHAs will also be time limited to 12 months. For employees who have been receiving LAFHAs under the transitional rules, the 12 month period is deemed to have started on 1 October 2012.

If the employee is working on a fly-in- fly-out or drive-in drive-out basis the LAFHA is not subject to the 12 month limit.

SMSFs

- **New SMSF trustee penalties** – from 1 July 2014 the ATO has greater powers to enforce the superannuation rules by levying financial penalties directly on trustees.
- **Concessional contribution cap changes** – from 1 July 2014 the concessional contribution cap for taxpayers up to the age of 50 is $30,000, and for those 50 and above the cap is $35,000.
- **Non-concessional cap changes** – the non-concessional contributions cap from 1 July 2014 is $180,000 (up from $150,000) or $540,000 over three years.
- **Insurance inside an SMSF** – from 1 July 2014 new insurance policies within an SMSF must be consistent with the death, terminal illness and permanent and temporary incapacity conditions of release in the Superannuation Industry (Supervision) Act.

Top 5 Simple Tax Saving Strategies

Planning on giving to charity? Make a donation now and claim the deduction this year. If you donate monthly to charities, think about paying the full year's worth of donations upfront and take the deduction now.

Operate through a company? If you operate through a company structure and the company has advanced you money during the year or paid expenses on your behalf, then work out whether you are going to repay the loans or put in place a complying loan arrangement. If you already have loan agreements in place from prior years, make sure that you make the minimum repayment (including interest) before 30 June. If the company normally declares a dividend to cover these loan repayments, make sure the dividend is declared and set off against the loan balance before 30 June.

Are your salary sacrifice agreements still relevant? If you have existing salary sacrifice agreements in place, review them to make sure they are still viable. Also, if your taxable income is over $180,000, don't forget about the debt tax (see the article on page 1 of this newsletter "Can You Plan Around the Debt Tax").

For business, if cash flow allows, now is the time to accelerate deductions by paying for any required repairs, replenishing consumable supplies, trade gifts or donations before 30 June.