



“What does it mean?”

On 24 November 2007, the Labor party became the new Government in Australia. In this Election Brief, we discuss the major announcements made by the Labor party during the election campaign, the impacts on your clients and the financial planning industry in general.

Taxation

In addition to supporting the personal tax cuts announced back in the 2007 Federal Budget, the Labor party has announced its intention to make further reforms over a six year period with the main impacts being:

- A personal taxation regime with only three marginal rates – 15%, 30% and 40%
- An increase in the low income tax offset to eventually lift the effective tax-free threshold from \$11,000 to \$20,000 by 2013/14

The proposed changes are summarised in the table below.

The fringe benefits tax rate will also be reduced from 1 July 2013 to a rate of 41.5% to match the change in the highest marginal tax rate. For those earning below \$180,000, these changes will raise a concern about the value of salary packaging arrangements. However, this is not to say that they aren't still appropriate. There will, for example, still be short and long term benefits in salary sacrificing to superannuation where the individual's average personal tax rate is above 15%.

These significant reforms to Australia's personal marginal tax rate system will

have the result of increasing the level of disposable income (after tax) that an individual will have. The question then will be what people choose to do with this extra money.

As has been the case with previous changes to the marginal tax rates, an important role for the financial planning industry will be to ensure that clients are prepared for when this “extra” money starts to come in and are equipped with the knowledge about appropriate investment options to ensure it is put to the best use for each particular individual.

Education

Labor have announced the introduction of an “education tax refund”. Under this proposal, eligible parents will be able to claim:

- a 50% refund each year for up to \$750 of education expenses for primary school children (a maximum benefit of \$375 per child per year), and
- a 50% refund each year for up to \$1,500 of education expenses for secondary school children (a maximum benefit of \$750 per child per year).

Current		From 1 July 2008		From 1 July 2009		From 1 July 2010		From 1 July 2013	
Taxable income	Rate	Taxable income	Rate	Taxable income	Rate	Taxable income	Rate	Taxable income	Rate
0- \$6,000	0%	0- \$6,000	0%	0- \$6,000	0%	0- \$6,000	0%	0- \$6,000	0%
\$6,001 - \$30,000	15%	\$6,001 - \$34,000	15%	\$6,001 - \$35,000	15%	\$6,001 - \$37,000	15%	\$6,001 - \$37,000	15%
\$30,001 - \$75,000	30%	\$34,001 - \$80,000	30%	\$35,001 - \$80,000	30%	\$37,001 - \$80,000	30%	\$37,001 - \$180,000	30%
\$75,001 - \$150,000	40%	\$80,001 - \$180,000	40%	\$80,001 - \$180,000	38%	\$80,001 - \$180,000	37%	\$180,001+	40%
\$150,001+	45%	\$180,001+	45%	\$180,001+	45%	\$180,001+	45%		

Families in receipt of Family Tax Benefit (Part A) will be eligible for this refund, and eligible expenditure covers costs associated with:

- laptops
- home computers and associated costs
- home internet connections
- printers
- education software and
- student school books

Importantly, this measure has been described as a refund, rather than a tax deduction, which means that all eligible people will obtain the same potential benefit, rather than the value of it differing depending on the individual's marginal tax rate.

From a financial planning perspective, it will be important to see how the mechanics of the actual refund work and how clients utilise it. For example, do they approach Centrelink to seek a direct refund of the relevant amount, or do they wait until the end of the year and use the entitlement to directly offset their taxation liability – both options currently available in relation to Family Tax Benefit (Part A).

Child care

The child care tax rebate will be lifted to 50%, covering a maximum of \$7,500 per child per year of child care costs. At the same time, investments will be made in making child care centres more available at education sites (such as TAFE and University) thus allowing parents to train to re-enter the workforce if they so desire.

This increase in rebate and increase in availability of child care centres may lead to increased levels of disposable income for families for which investment advice may be needed.

Housing

One of the largest financial planning issues facing many clients (and not just those of the younger generations) is working out how to afford their first home – when and how to start saving towards the deposit and maximising it to reduce the need for mortgage insurance and the impact of potential interest rate increases.

To this end, the Labor party have announced they will introduce “First Home Saver Accounts” (FHSA), available to people over 18 who meet the eligibility criteria for the First Home Owners Grant (FHOG).

The FHSA will be a superannuation style account, although it will operate independently of any superannuation account the person may have. Up to \$10,000 (indexed annually) may be contributed to the account, with:

- a maximum of \$5,000 (indexed) being contributed from pre-tax income. This will operate like a superannuation salary sacrifice arrangement, with 15% tax being deducted from these contributions; and
- the balance able to be contributed from after tax contributions. This may be made by the individual or a third party.

Earnings in the account will be taxed at the superannuation rate of 15%. If invested in shares paying franked dividends, the FHSA will receive the benefit of imputation credits, reducing the effective rate of tax payable.

The minimum time frame for operation of the FHSA is 4 qualifying years, with a minimum initial deposit of \$1,000. Only those years in which a minimum of \$1,000 is deposited will count as a qualifying year. The maximum level of deposits (contributions) that can be made into a FHSA is \$50,000.

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Withdrawals from the FHSA will only be permitted after the 4 year qualifying period has been satisfied and only where the amount is used towards the purchase of a first home that also qualifies for the FHOG. It is paid tax-free and in addition to the FHOG. Other withdrawals will only be permitted in exceptional circumstances (such as severe financial hardship or on certain illness grounds). Any unused balance may be rolled into the individuals existing superannuation account, and will be subject to the standard preservation rules.

The introduction of the FHSA offers financial advisers new ways to educate clients about savings, including:

- a mechanism to save towards the ‘great Australian dream’ of owning your own home
- introduce a disciplined approach to savings with a specific goal in mind
- prepare clients for the continuation of a salary sacrifice arrangement to superannuation once the maximum level of pre-tax contributions to the FHSA have been reached

- to the extent the FHSA is not used entirely towards the deposit on a home, give a kick-start to the client's future retirement savings goals.

In addition, with the post-tax contributions able to be made by third parties, it is a mechanism for parents (and possibly grand-parents) to be able to provide some assistance to children (or grand-children) in a tax advantaged method with some certainty on how the money will actually be spent. Future contributions could be specified in a client's will to be made to the FHSA of specific beneficiaries once they turn 18.

Superannuation

The Labor party supported the passage of the Simpler Superannuation reforms and it is not expected that any significant changes will be made to the new rules that have been in place since 1 July this year. However, there are some other initiatives that have been mentioned by the Labor party in relation to superannuation and its operation.

A centralised clearing house

Rather than employers making super guarantee payments to different superannuation funds for different members, Labor has proposed the establishment of one central clearing house to receive these payments. The clearing house would then distribute these amounts to the relevant funds for the employees concerned.

The service would be free for small businesses (those with 20 employees or less) and subject to a charge for larger businesses. Labor believes this facility will reduce the incidence of lost superannuation accounts.

The operation of this account may make it easier for employees when they change job, as their "choice of fund" election is always made to the one clearing house, rather than potentially changing each time they change

employment. However, if the clearing house only operates in relation to super guarantee payments, concerns will still arise over how additional salary sacrificed contributions are dealt with.

Tax-free payments on terminal illness

Prior to calling the election, the Coalition announced that it would legislate to allow payments from superannuation to members suffering from a terminal illness to be made tax-free. The Labor party supported this announcement, and the relevant amendments to the legislation and regulations will be expected when Parliament resumes.

It will be important to ensure that amendments are also made to the relevant superannuation regulations to introduce terminal illness as a new condition of release from superannuation. Without this important change, those under preservation age suffering from a terminal illness will not be able to access these tax-free benefits unless they are also permanently incapacitated – which may not be the case for many of them.

Changes to superannuation guarantee arrangements

There has long been agreement that sustained superannuation savings and contributions at the legislated 9% super guarantee (SG) level will not be sufficient to allow Australians to be truly self-funded in retirement. There is general agreement that a more appropriate level is 15% of annual pre-tax income.

In the past, there has much talk that a Labor Government would look to increase the SG from 9% to 15%, with the increase to be funded equally by employers (through lifting the SG requirement to 12%) and employees (by introducing a compulsory personal component of 3%).

The cost of such a measure would be significant and it is not expected that such a change will be introduced by a Labor Government, at least not in its first term in office.

What is expected however, is a change to how the SG requirement is calculated. Currently, SG is payable only on the "cash component" of a person's wage – that is after reducing a base salary for any salary packaged amounts. It is anticipated that SG will become payable on a base salary amount before any packaging is done.

For example, an employee today may be on a base salary of \$100,000. If no packaging is undertaken, SG payable is \$9,000. If the employee however decided to salary sacrifice \$10,000 to super, their cash component is reduced to \$90,000 and the SG liability is only \$8,100. Some employers may also state that the \$10,000 salary sacrificed is an employer contribution and therefore meets their SG obligation (which under current law it does) and therefore make no additional contribution to super.

Under the anticipated changes, in the example above, the employer would be required to contribute the \$9,000 in SG in all scenarios, in addition to any salary sacrificed amounts.

Such a change would be beneficial, not only in assisting clients to build their superannuation savings, but also in ensuring consistency between employers in how SG liabilities are calculated and making it simpler for employees to understand.

Social security

Amongst other measures, Labor has announced its intention to introduce:

- a quarterly Utilities Allowance of \$125 to older Australians in receipt of income support payments such as the Age Pension and Veterans Service Pension. This equals a total annual payment of \$500 for singles and \$500 for a couple;

- a similar payment for people receiving Carer Payment or the Disability Support Pension. This equals a total annual payment of \$500 for singles and \$500 for a couple; and
- a quarterly Seniors Concession Allowance of \$125 per person to eligible self-funded retirees. This equals a total annual payment of \$500 for each eligible individual.
- Facilitating the provision of good financial advice on a cost-effective basis. This may involve reviewing certain aspects of the FSR regime to make it easier to provide limited advice to clients.
- The requirement for consistent forecasting models to be provided by superannuation funds to enable members to gain an understanding of their future level of retirement savings based on certain assumptions.

Other proposals

Whilst not necessarily announced in the election campaign, there are other proposals that the Labor party have announced over time that may make an appearance during the first or subsequent terms of a Labor Government that will impact on the financial planning industry. These include:

- The establishment of a single regulator for the financial services industry. This would involve a merger of some of the functions and activities of ASIC and APRA.
- The abolition of exit fees on investor accounts. Whether or not this would apply only to new accounts established or include existing accounts is yet to be seen.

Conclusion

It is important to remember that none of these measures have yet been legislated and it is not expected that Parliament will resume until the new year. The constitution of the Senate will also be important in relation to the passage of new legislation, with the Coalition still retaining its Senate majority until 1 July 2008.

If you have any questions please contact Technical Services on 1800 655 901 or email tech_services@asgardwealthsolutions.com.au

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