MARTIN & ORR

ACCOUNTANTS

Practice Update: Special Edition

May 2021

2021 Budget Report

1. Personal income tax changes

1.1 Retaining the Low and Middle Income Tax Offset ('LMITO') for the 2022 income year

The Government has announced that it will retain the LMITO for one more income year, so that it will still be available for the 2022 income year. Under current legislation, the LMITO was due to be removed from 1 July 2021.

The LMITO is a non-refundable tax offset that provides tax relief for low and middle income taxpayers and is available in addition to the Low Income Tax Offset ('LITO').

The LMITO is proposed to apply as follows for the 2022 income year.

Proposed LMITO for 2022	
$37,000 or less	Up to $255
$37,001 to $48,000	$255 + 7.5% of excess over $37,000
$48,001 to $90,000	$1,080
$90,001 to $126,000	$1,080 – 3% of excess over $90,000
$126,001+	Nil

Consistent with current arrangements, the LMITO will be applied to reduce the tax payable by individuals when they lodge their tax returns for the 2022 income year.

1.2 Increasing the Medicare levy low-income thresholds

The Government will increase the Medicare levy low-income thresholds for singles, families and seniors and pensioners for the 2021 income year, as follows:

- The threshold for **singles** will be increased from $22,801 to $23,226.
- The **family** threshold will be increased from $38,474 to $39,167.
- The threshold for **single seniors and pensioners** will be increased from $36,056 to $36,705.
- The **family** threshold for **seniors and pensioners** will be increased from $50,191 to $51,094.

For each dependent child or student, the family income thresholds increase by a further $3,597, up from the previous amount of $3,533.

1.3 Updating individual tax residency rules

The Government has announced that it will replace the individual tax residency rules with a new framework.

The **primary test** will be a simple 'bright line' test – a person who is physically present in Australia for 183 days or more in any income year will be an Australian tax resident.

Individuals who do not meet the primary test will be subject to **secondary tests** that depend on a combination of physical presence and measurable, objective criteria.

Australia's current tax residency rules are difficult to apply in practice, creating uncertainty and resulting in high compliance costs for individuals and their employers.

The new framework is based on recommendations made by the Board of Taxation in its 2019 report to Government, *'Reforming individual tax residency rules – a model for modernisation'*. According to the Government, this new framework will be easier to understand and apply in practice, deliver greater certainty, and lower compliance costs for globally mobile individuals and their employers.

This measure will have effect from the first income year after the date of Royal Assent of the enabling legislation.

1.4 Reducing compliance costs for individuals claiming self-education expense deductions

The Government will remove the exclusion of the first $250 of deductions for prescribed courses of education.

Currently, the first $250 of a prescribed course of education expense is not tax deductible. Removing this $250 exclusion is expected to reduce compliance costs for individuals claiming self-education expense deductions.

This measure will have effect from the first income year after the date of Royal Assent of the enabling legislation.

1.5 Employee Share Schemes – removing 'cessation of employment' as a taxing point

The Government will **remove** the 'cessation of employment' taxing point for tax-deferred Employee Share Schemes ('ESS') that are available for all companies.

This change will apply to ESS interests issued from the first income year after the date of Royal Assent of the enabling legislation.

Currently, under a tax-deferred ESS, where certain criteria are met, employees may defer tax until a later tax year ('the deferred taxing point'). The deferred taxing point is the earliest of:

a) cessation of employment;

b) in the case of shares, when there is no risk of forfeiture and no restrictions on disposal;

c) in the case of options, when the employee exercises the option and there is no risk of forfeiting the resulting share and no restriction on disposal; and

d) the maximum period of deferral of 15 years.

This change will remove the 'cessation of employment' taxing point (i.e. point (a) above) and result in tax being deferred until the earliest of the remaining taxing points (i.e. points (b) to (d) above).

In addition to this change, the Government will also reduce administrative requirements for ESS:

- where employers do **not** charge or lend to the employees to whom they offer ESS – by removing regulatory requirements for ESS; and

- where employers **do** charge or lend – by streamlining requirements for unlisted companies making ESS offers that are valued at up to $30,000 per employee per year.

This measure aims to help Australian companies to engage and retain the talent they need to compete on a global stage, consistent with recommendations from the Global Business and Talent Attraction.

1.6 Exemption for pay and allowances for Operation Paladin

The Government will provide a full income tax exemption for the pay and allowances of Australian Defence Force ('ADF') personnel deployed to Operation Paladin.

Operation Paladin is Australia's contribution to the United Nations Truce Supervision Organisation, with ADF personnel deployed in Israel, Jordan, Syria, Lebanon and Egypt.

This measure ensures that personnel are subject to consistent tax treatment regardless of the operational area of Operation Paladin to which they are deployed.

The exemption will apply **from 1 July 2020** (i.e. from the start of the 2021 income year).

2. Changes affecting business taxpayers

2.1 Temporary full expensing extension

In the prior year's (2020/21) Federal Budget, the Government announced amendments to allow businesses with an aggregated turnover of *less than* $5 billion to access a new temporary full expensing of eligible depreciating assets until 30 June 2022. Temporary full expensing became law when *Treasury Laws Amendment (A Tax Plan for the COVID-19 Economic Recovery) Bill 2020* received Royal Assent on 14 October 2020.

In the 2021/22 Federal Budget, the Government has announced that temporary full expensing will be extended by 12 months to allow eligible businesses with aggregated annual turnover or total income of less than $5 billion to deduct the full cost of eligible depreciable assets of any value, acquired from 7:30pm AEDT on 6 October 2020 and first used or installed ready for use by 30 June 2023. All other elements of temporary full expensing will remain unchanged, including the alternative eligibility test based on total income, which will continue to be available to businesses.

2.2 Temporary loss carry-back extension

In the prior year's (2020/21) Federal Budget, the Government announced amendments to introduce a temporary loss carry-back measure. Broadly, this initial measure allowed 'corporate tax entities' with an aggregated turnover of *less than* $5 billion to carry back tax losses made in the 2020, 2021 and/or 2022 income years to claim a refund of tax paid (by way of a tax offset) in relation to the 2019, 2020 and/or 2021 income years. The rules relating to the temporary loss carry-back regime have been enacted and are contained in Division 160 of the ITAA 1997.

In the 2021/22 Federal Budget, the Government has announced that the loss carry-back measure will be extended to allow eligible companies (i.e., with aggregated turnover of less than $5 billion) to also carry back (utilise) tax losses from the 2023 income year to offset previously taxed profits as far back as the 2019 income year when they lodge their tax return for the 2023 income year.

Consistent with the current law, the tax refund available under this measure is limited by requiring that the amount carried back is not more than the earlier taxed profits and does not generate a franking account deficit. Companies that do not elect to carry back losses under this measure can still carry losses forward as normal.

2.3 Digital economy strategy (including self-assessing the effective life of intangible depreciating assets)

The Government will provide $1.2 billion over six years from 2022 for the Digital Economy Strategy, to develop Australia's digital economy by 2030. From an income tax and investment incentive perspective, the Digital Economy Strategy includes the following:

(a) The Government will allow taxpayers to self-assess the tax effective lives of eligible intangible depreciating assets, such as patents, registered designs, copyrights and in-house software. This measure will apply to assets acquired from 1 July 2023, after the temporary full expensing regime has concluded.

The tax effective lives of such assets are currently set by statute. Allowing taxpayers to self-assess the tax effective life of an asset will allow for a better alignment of tax outcomes with the underlying economic benefits provided by the asset. It will also align the tax treatment of these assets with that of most tangible assets.

Taxpayers will continue to have the option of applying the existing statutory effective life to depreciate these assets.

(b) The Government will provide $18.8 million over four years from 2022 for a Digital Games Tax Offset to provide a 30% refundable tax offset for qualifying Australian digital games expenditure ongoing from 1 July 2022, with the criteria and definition of qualifying expenditure to be determined through industry consultation.

(c) The Government will provide $200.1 million over two years from the 2022 income year to develop and transition government services to a new myGov platform, providing a central place for Australians to find information and services online.

2.4 Debt recovery for small business

The Government has announced that it will allow small business entities (including individuals carrying on a business) with an aggregated turnover of less than $10 million per year to apply to the Small

Business Taxation Division of the Administrative Appeals Tribunal (the 'Tribunal') to pause or modify ATO debt recovery actions, such as garnishee notices and the recovery of general interest charge or related penalties, where the debt is being disputed in the Tribunal.

Currently, small businesses are only able to pause or modify ATO debt recovery actions through the court system, which can be costly and time consuming. It is expected that applying to the Tribunal instead of the courts will save small businesses at least several thousands of dollars in court and legal fees and as much as 60 days of waiting for a decision.

These new powers for the Tribunal will be available in respect of proceedings commenced on or after the date of Royal Assent of the enabling legislation.

2.5 Tax treatment of qualifying storm and flood grants

The Government will provide an income tax exemption for qualifying grants made to primary producers and small businesses affected by the storms and floods in Australia.

Qualifying grants are Category D grants provided under the *Disaster Recovery Funding Arrangements 2018*, where those grants relate to the storms and floods in Australia that occurred due to rainfall events between 19 February 2021 and 31 March 2021. These include small business recovery grants of up to $50,000 and primary producer recovery grants of up to $75,000. The grants will be made non-assessable non-exempt income for tax purposes.

3. Superannuation related changes

3.1 Removing the work test for voluntary contributions

The Government has announced that it will allow individuals aged 67 to 74 years (inclusive) to make or receive non-concessional contributions (including under the bring-forward rule) and salary sacrifice contributions without meeting the work test, subject to existing contribution caps.

Individuals aged 67 to 74 years (inclusive) will still have to meet the work test to make personal deductible contributions.

The measure will have effect from the start of the first income year after Royal Assent of the enabling legislation, which the Government expects to have occurred prior to 1 July 2022.

Currently, individuals aged 67 to 74 years (inclusive) can only make voluntary contributions (both concessional and non-concessional) to their superannuation fund, or receive contributions from their spouse, if they satisfy the work test (subject to a limited work test exemption). Generally, to satisfy the work test, an individual must be working for at least 40 hours over a period of not more than 30 consecutive days in the income year the relevant contribution is made.

Removing the requirement to meet the work test when making non-concessional or salary sacrifice contributions will simplify the rules governing superannuation contributions and will increase flexibility for older Australians to save for their retirement through superannuation.

3.2 Reducing the age limit for downsizer contributions

The Government will reduce the age limit from which downsizer contributions can be made by eligible individuals, from 65 to 60 years of age.

The measure will have effect from the start of the first income year after Royal Assent of the enabling legislation, which the Government expects to have occurred prior to 1 July 2022.

The downsizer contribution allows eligible individuals to make a one-off, after-tax contribution to their superannuation fund, of up to $300,000 per person, following the disposal of an eligible dwelling, where certain conditions are satisfied. Under the current requirements, an individual must be at least 65 years of age at the time of making the relevant contribution, for the contribution to qualify as a downsizer contribution.

3.3 Removing the $450 per month threshold for Superannuation Guarantee ('SG') eligibility

The Government will remove the current $450 per month minimum income threshold, under which employees do not have to be paid SG contributions by their employer.

The measure will have effect from the start of the first income year after Royal Assent of the enabling legislation, which the Government expects to have occurred prior to 1 July 2022.

3.4 Loosening the residency requirements for Self-managed Superannuation Funds ('SMSFs')

The Government will relax residency requirements for SMSFs and small APRA-regulated funds by:

- extending the central control and management test safe harbour from two years to five years for SMSFs; and
- removing the active member test for both types of funds.

The measure will have effect from the start of the first income year after Royal Assent of the enabling legislation, which the Government expects to have occurred prior to 1 July 2022.

This measure will allow SMSF members and small APRA fund members to continue to contribute to their superannuation fund whilst temporarily overseas, ensuring parity with members of large APRA regulated funds.

3.5 Exiting legacy retirement products

The Government has announced that it will allow individuals the temporary option to exit and convert from a specified range of legacy retirement products (together with any associated reserves) into more flexible and contemporary retirement products, for a two-year period.

The products covered by this measure include market-linked, life-expectancy and lifetime products that were first commenced before 20 September 2007 from any provider (including an SMSF), but **not** flexi-pension products or a lifetime product in a large APRA-regulated or public sector defined benefit scheme.

The measure will have effect from the first income year after the date of Royal Assent of the enabling legislation.

Currently, these products can only be converted into another like product and limits apply to the allocation of any associated reserves without counting towards an individual's contribution caps.

This measure will permit full access to all of the product's underlying capital, including any reserves, as part of transitioning into a more flexible and contemporary retirement product.

Social security and taxation treatment will not be grandfathered for any new products commenced with commuted funds, and the commuted reserves will be taxed as an assessable contribution.

3.6 Changes to the First Home Super Saver ('FHSS') scheme

The Government has announced that it will make the following changes to the FHSS scheme:

3.6.1 Increasing the maximum releasable amount to $50,000

The Government will increase the maximum releasable amount of voluntary concessional and non-concessional contributions under the FHSS scheme from $30,000 to $50,000, to assist first home buyers in raising a deposit more quickly.

Voluntary contributions made from 1 July 2017 up to the existing limit of $15,000 per year will count towards the total amount able to be released.

This change will apply from the start of the first income year after Royal Assent of the enabling legislation, which the Government expects will have occurred by 1 July 2022.

Under the current FHSS scheme, an eligible individual can apply to have a maximum of $15,000 of their voluntary contributions from any one income year included in their eligible contributions to be released under the FHSS scheme, up to a total of $30,000 contributions across all years, together with an amount of earnings that relate to those contributions.

3.6.2 Changes to the operation of the FHSS scheme

The Government will make four technical changes to the legislation underpinning the FHSS scheme to improve its operation as well as the experience of first home buyers using the scheme.

These four changes will apply retrospectively from 1 July 2018, and will assist FHSS scheme applicants who make errors on their FHSS scheme release applications by:

• increasing the discretion of the Commissioner of Taxation to amend and revoke FHSS scheme applications;

• allowing individuals to withdraw or amend their applications before receiving a FHSS scheme amount, and allow those who withdraw to re-apply for FHSS scheme releases in the future;

• allowing the Commissioner of Taxation to return any released FHSS scheme money to superannuation funds, provided that the money has not yet been released to the individual; and

• clarifying that the money returned by the Commissioner of Taxation to superannuation funds is treated as a fund's non-assessable non-exempt income and does not count towards the individual's contribution caps.

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