

FEDERAL BUDGET 2019 / KEY ANNOUNCEMENTS

On 2 April 2019, Treasurer Josh Frydenberg delivered Australia’s federal budget for 2019-20. Coming ahead of a likely May federal election, the budget lays the foundation for the government’s re-election campaign, and highlights the Coalition’s economic management with the first budget-year surplus in over a decade. The budget also promises significant personal income tax cuts along with significantly increased funding for small businesses, infrastructure and a range of essential services.

In the following update, we provide a summary of the key announcements from the budget from the perspective of investors and briefly outline the potential economic impacts.

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Changes to personal income tax

The government has announced a \$158 billion tax relief package, estimating some 10 million taxpayers will benefit from reduced marginal tax rates and adjusted low-income tax offset.

From 2018-19, the government will further reduce taxes for low and middle-income earners who will have their tax reduced by up to \$1,080 for single earners or up to \$2,160 for dual income families.

In 2022-23, the government will increase the top threshold of the 19% tax bracket from \$41,000 to \$45,000 and increase the low-income tax offset from \$645 to \$700.

In 2024-25, the government will reduce the 32.5% tax rate to 30%, which aligns the middle tax bracket more closely with corporate tax rates and the 37% tax rate will be eliminated.

The rate reduction builds on the changes the government has already legislated—increasing the top threshold of the middle tax bracket from \$120,000 to \$200,000 and abolishing the 37% tax bracket. This will result in a simpler system comprising three tax rates: 19%, 30% and 45%.

New personal tax rates and thresholds (excluding Medicare)

	CURRENT THRESHOLDS	NEW THRESHOLDS FROM 2018-19 TO 2021-22	NEW THRESHOLDS FROM 2022-23 TO 2023-24
Tax-free	0-18,200	0-18,200	0-18,200
19	18,201-37,000	18,201-37,000	18,201-45,000
32.5	37,001-87,000	37,001-90,000	45,001-120,000
37	87,001-180,000	90,000-180,000	120,001-180,000
45	>180,000	>180,000	>180,000
INCOME TAX OFFSETS (\$)			
Low-income tax offset	Up to 445	Up to 445	Up to 700
Low and middle-income tax offset		Up to 1,080	
		NEW THRESHOLDS FROM 2024-25	
Tax-free	0-18,200		
19	18,201-45,000		
30	45,001-200,000		
45	>200,000		
INCOME TAX OFFSETS (\$)			
Low-income tax offset	Up to 700		

Medicare levy low-income threshold

The government will increase the Medicare levy low-income thresholds from the 2018-19 income year, allowing low-income taxpayers to continue to be exempted from paying the Medicare levy.

- **Single**—threshold will increase from \$21,980 to \$22,398.
- **Family**—threshold will increase from \$37,089 to \$37,794.
- **Single seniors and pensioners**—threshold will increase from \$34,758 to \$35,418.
- **Family threshold for seniors and pensioners**—will increase from \$48,385 to \$49,304.

Small to medium business tax

The government has fast-tracked its legislated tax cuts for small and medium-sized businesses by bringing those tax cuts forward so that the plan is fully implemented by 2021-22, five years earlier than expected.

Increasing the instant asset write-off threshold—From Budget night to 30 June 2020, the threshold increases from \$25,000 to \$30,000. Further, the government has expanded access to the instant asset write-off from small businesses with less than \$10 million turnover to medium-sized businesses with annual turnover less than \$50 million. The threshold applies on a per asset basis allowing instant write off of multiple assets.

Fast-tracking the company tax rate cut—Small and medium-sized companies with turnover of less than \$50 million will receive a tax cut from 27.5% to 25% by 2021-22.

Superannuation

Non-concessional contributions for those aged 65 and 66

From 1 July 2020, individuals aged 65 and 66 will have the ability to make voluntary concessional and non-concessional contributions without needing to meet the work test (i.e. 40 hours in a 30-day consecutive period in the financial year). This is expected to still be subject to the general Total Super Balance Cap rules which limit the level of non-concessional superannuation contributions for a member with a total super balance of \$1.6 million.

Further, the 'bring-forward' arrangements, which are currently limited to individuals aged under 65, allowing three years' worth of non-concessional contributions, will be extended to those aged 65 and 66.

CONTRIBUTION TYPE	CURRENT UP TO AGE 64	CURRENT AGE 65-74	PROPOSED FROM 1/7/2020 UP TO AGE 66	PROPOSED FROM 1/7/2020 AGE 67-74
Non-concessional contribution cap	100,000	100,000 ¹	100,000 ²	100,000 ³
Bring-forward NCC	300,000	N/A	300,000	N/A
Concessional cap	25,000	25,000 ¹	25,000 ²	25,000 ³

1. Work test of 40 hours within 30-day consecutive period needs to be met prior to contribution being made.
2. Work test does not need to be met in order to be eligible to make contribution.
3. Work test needs to be met prior to contribution being made.

Spouse contributions

Currently, member contributions can be made on behalf of a spouse under the following circumstances:

- The receiving spouse is under the age of 65; or
- the receiving spouse is age 65 to 69 and has satisfied the 'work test'.

The upper age limit for spouse contributions to super will increase from the age of 69 to 74, with those aged 65 and 66 no longer needing to meet the work test.

Providing the eligibility criteria is met, a spouse contribution can provide the contributing member with a tax offset of up to \$540.

Aligning the work test with the eligibility age for the Age Pension (scheduled to reach 67 from 1 July 2023) and increasing the age limit for spouse contributions to 74 will give older Australians greater flexibility to save for retirement.

Protecting Your Super Package

Insurance opt in

With regards to ensuring that insurance within superannuation is only offered on an 'opt-in' basis for accounts with balances of less than \$6,000 and new accounts belonging to members under the age of 25 years, the government will delay the start date to 1 October 2019.

These changes, which are currently before Parliament, will protect the retirement savings of young people and those with low balances by ensuring their superannuation is not unnecessarily eroded by premiums on insurance policies they do not need or are not aware of. The changes will also reduce the incidence of duplicated cover so that individuals are not paying for multiple insurance policies which they may not be able to claim on. These changes will not prevent anyone who wants insurance from being able to obtain it—low balance members and young members will still be able to opt in to insurance cover within superannuation.

Inactive super accounts

The government has agreed to amendments to the Protecting Your Super Package as announced in the 2018-19 Budget to:

- extend to 16 months the period after which an account that has not received any contribution is considered inactive;
- expand the definition of when an account is considered active for the Australian Taxation Office-led consolidation regime; and
- require the Australian Taxation Office to consolidate to an active account, where possible, within 28 days of receipt.

Tax integrity

Further consultation to Div 7A amendments—reforms delayed

The start date of amendments to Div 7A of the *Income Tax Assessment Act 1936* will be delayed by 12 months to 1 July 2020.

The proposed amendments previously announced will undergo further consultation following a consultation paper issued in October 2018. The amendments included replacing the existing seven-year and 25-year model with a single 10-year model without a requirement for a formal written loan agreement and clarification as to when unpaid present entitlements come within the scope of Div 7A.

What does it mean for investors?

This year's federal budget continues to benefit from an underlying improvement in revenue, largely reflecting stronger-than-expected jobs growth and higher-than-forecast commodity prices. Lower government spending (helped by ongoing low inflation) was also a significant contributor to an improved fiscal outlook. But consistent with past pre-election budgets, much of the additional revenue has been returned to the economy by:

- providing significant additional personal income tax cuts to low and middle-income earners;
- boosting spending on infrastructure; and
- increasing funding for small businesses, as well as health, aged care and education sectors.

All in all, the budget bottom line continues to reveal a steadily improving fiscal outlook, based on reasonable forecasts, with 2019-20 delivering the first budget surplus in over a decade. The budget also commits to reducing Australia's net debt to zero by 2029-30. Despite this, the budget is modestly stimulatory (arguably less stimulatory than expected), supporting growth by a little less than 0.2% of GDP per year over the next couple of years. Given the recent significant slowing in Australia's growth rate and an unnecessary rise in the tax-to-income ratio, this stimulus is arguably a better and more powerful policy prescription than applying further cuts to interest rates that are already at record lows. According to CBA, the \$7.2 billion of tax cuts slated for 2019-20 and 2020-21 would have nearly the same impact on disposable income as two 25 basis point cuts to official rates.

How are markets likely to react?

The budget is likely to be relatively well received by markets. However, the prospect of an imminent election (and a potential change in government) may mute any reaction. Still, sectors linked to the consumer, small business capex, health services and infrastructure are likely to benefit most—particularly given expected bipartisan support in these policy areas from the opposition Australian Labor Party (ALP). A planned return to zero net debt could support bond markets over time. In addition, the maintenance of sustained surpluses strengthens Australia's AAA rating and is a positive for the Australian dollar.

Consumer sectors to benefit from lower tax burdens and reduced cost of services

The budget contains significant personal income tax cuts (\$158 billion over 10 years), focused on reducing tax rates and increasing thresholds from 2022. But a doubling of the low and middle-income tax offset from \$530 to \$1,080 per person (to start early next financial year) adds to household income more quickly, as do modest cash handouts (\$75 per welfare recipient) to offset rising energy bills. Households also benefit from greater access to, and reduced costs of, some medical services.

The budget immediately increases the small business instant asset write-off, while also extending it to multiple assets, as well as to medium-sized businesses. This will support near-term demand for motor vehicles, technology products, office equipment and the like. The small business tax rate is also lowered from 2021 (from 27.5% to 25.0%).

Additional \$25 billion upgrade to infrastructure should support capex and materials sectors

The infrastructure sector will benefit from an additional \$6.2 billion of increased spending over the next four years, bringing the current program to \$100 billion over the next decade (up from \$75 billion in the previous budget). Road and rail projects remain the focus, including an additional \$3 billion to tackle congestion. New projects include \$2 billion for a Geelong to Melbourne fast train, \$1.6 billion for new highway and bridge upgrades in Western Australia, \$4 billion in Queensland, which includes upgrades to the Bruce Highway and Gateway Motorway, while New South Wales and Victoria receive \$7.3 billion and \$6.2 billion respectively for various road and rail projects. Infrastructure spending remains a key support for the economy as the housing sector correction unfolds.

Health and aged care sectors benefit from increased funding

The budget increases spending on health, including additional funding for diagnostic imaging, increasing Medicare rebates for some GP services, increasing funding for community hospitals, as well as adding new listings to the Pharmaceutical Benefits Scheme. It also increases funding to in home care, so a further 10,000 aged care recipients can receive their care at home, while also making an additional 13,500 residential care places available and providing \$60 million for residential care infrastructure. The Medical Research Future Fund also receives an additional \$5 billion.

Banks to face increased levies to fund Hayne Banking Royal Commission recommendations

The budget provides for around \$600 million over five years to facilitate the government's response to the Hayne Banking Royal Commission. This is likely to be ultimately funded by increased levies on the banking sector, not dissimilar to the ALP's already proposed \$640 million 'fairness' fund tax over four years.

Other sectors that benefit

The vocational education sector benefits from additional funding, as does pre-school funding for places from 2020. The budget also pledges almost half a billion dollars to a mental health and suicide prevention strategy, and an extra 80,000 apprenticeships as part of a skills package for young workers. The budget also includes \$6.3 billion in assistance and concessional loans to those affected by drought and \$3.3 billion to those affected by floods. There were modest benefits to the superannuation sector, with some tweaks to last year's 'Protecting Your Superannuation' package also announced, including allowing additional superannuation contributions at age 65 and 66 without meeting work tests. In contrast, research and development funding has been cut, while multi-national corporations are a key focus of the budget's tax avoidance savings.

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