Grant Thornton

Building a new path

FEDERAL BUDGET 2022

Insights from the “Responsible Budget”

The second Federal Budget of the year has been delivered, and this time it’s a Budget that will be rolled out for the rest of FY22–23. Since the previous Government presented a Budget in March, the economy has shifted at an alarming rate with the cash rate rise from 0.1 per cent in March to 2.6 per cent now, and on its way to 3.1 per cent by the end of the year. Australia is experiencing the highest inflation in 40 years driving higher prices and forcing up interest rates, all as a result of war and escalating the risk of another global recession.

When a new Government delivers its first Budget, it sets the tone for its leadership. Since being elected, Labor has prepared Australians for a “solid and sensible” Budget where its “two–Budget” approach funds Government promises while also claiming to find $22b in savings over four years.

But what does this mean for your business? What do Australian businesses need to watch out for if we’re hurtling into a recession? How do the key spending highlights of the Budget address current and potential economic issues while helping Australian businesses maintain profitability?

Businesses have been impacted more than ever by the effects of climate change; first the bushfires and then flooding. These natural disasters have already come at a huge cost to the economy with $3b set aside in this Budget for natural disaster recovery with future costs to come. There is no escaping the effects the recent floods will have on inflation with fruit and vegetable prices likely to increase by 8 per cent by the end of the year.

In response, the Government has set an emissions target of a 43 per cent reduction in 2030 and net zero for 2050, however, we have not yet received any policies on how these targets will be achieved and who will actually pay for the targets to be realised.

Most mid-sized businesses are in a position where their stakeholders are demanding transparency and disclosure on their Environmental, Social and Governance (ESG) policies. As businesses aim to become carbon neutral and certified as net zero. It means increased requirements and extra costs which must be managed. Businesses are looking to Government to legislate compliance and mandate policies, as well as monetary assistance to cover costs and implementation.

In addition, our economy continues to suffer the effects of talent shortages creating a disconnect between the unemployment rate and the number of available skilled workers. Wages growth is at its lowest point in ten years. We hope the immigration measures to welcome skilled workers from overseas, and the Government's $1b investment in education to create additional training places boosts employment figures.

Governments have typically turned to taxes to generate revenue in the Budget and this time around, Labor's proposed Multinational Tax rates to rewrite certain tax laws could potentially recoup close to $1.1b that will make a significant dent in our overall debt. On the flipside, these restrictions on MNEs could deter their investment in Australian business.

The Government spoke about a future of Made in Australia and highlighted the key areas of manufacturing clean energy, medical manufacturing, new technologies, agriculture, and critical minerals. It's easy to talk about domestic manufacturing but, will the $15b National Reconstruction Fund have enough funds and clear direction for Australia to become more independent?

This is the fourth Budget delivered in the last two years which have mostly consisted of short-term reactions from Government to deal with the COVID-19 pandemic. This Budget was based on a rationale encompassing the effects of natural disasters, a deteriorating global economy, rising inflation, a shrinking workforce, and ongoing supply chain pressures. The commitments revealed in this budget are the starting point of a more sustainable budget expected in May 2023 and are underpinned by a long-term strategy.

Businesses are looking for real change and real improvements that go beyond the current news cycle. It will be interesting to see if these measures taken by the Government will help resolve the budget deficit and keep Australia's economy moving forward.

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PRIORITIES

- Health and Aged Care
- Childcare and Parental Leave
- Education, skills and training, and wages growth
- National Reconstruction Fund including disaster relief, support for farmers, and environmental initiatives
- Clean energy and Australian made manufacturing

Spending highlights

BUDGET DEFICIT

For 2021/22	$-32b
For 2022/23	$-36.9b
For 2023/24	$-44b
For 2024/25	$-51.3b
For 2025/26	$-49.6b

NET DEBT

For 2021/22	$515.6b
For 2022/23	$572.2b
For 2023/24	$634.1b
For 2024/25	$702.8b
For 2025/26	$766.8b

KEY SPENDING HIGHLIGHTS – A SNAPSHOT

$4.7b Over four years from 2022–23 to ease the costs of childhood education and care.

$531.6m Expand the Paid Parental Leave scheme from 18 to 26 weeks over four years from 2022–23.

$2.5b Implement Royal Commission recommendations including more nurses and safer living conditions, and additional $810m COVID-19 support.

$8.8b Increase in NDIS funding over four years.

$2.4b Investment in NBN over four years, and a further $1.2b for the Better Connectivity for Regional and Rural Australia Plan.

$10b For the Housing Australia Future Fund to deliver 30,000 social and affordable homes over five years from 2024.

$20b New Powering Australia Plan with low-cost finance for upgrades to the Australian electricity grid under Rewiring the Nation program.

$1.9b Powering the Regions Fund to transform regional industries through de-carbonisation.

$15b National Reconstruction Fund to finance projects that invest in sovereign manufacturing capabilities.

$1b Training package for 480,000 fee-free TAFE and community-based vocational training places.

195k Increase to the permanent migration cap from 160,000 to 195,000 to alleviate the skills shortage.

$7.4b To support regional development across Australia.

Tax

INTERNATIONAL TAX

Multinational Tax Integrity Package

Changes to thin capitalisation rules

Amending Australia's interest limitation (thin capitalisation) rules for income years commencing on or after 1 July 2023:

- Limit an entity's debt-related deductions to 30 per cent of profits (using EBITDA — earnings before interest, taxes, depreciation, and amortisation – as the measure of profit). This new earnings-based test will replace the safe harbour test
- Allow deductions denied under the entity-level EBITDA test (interest expense amounts exceeding the 30 per cent EBITDA ratio) to be carried forward and claimed in a subsequent income year (up to 15 years)
- Allow an entity in a group to claim debt-related deductions up to the level of the worldwide group's net interest expense as a share of earnings (which may exceed the 30 per cent EBITDA ratio). This new earnings-based group ratio will replace the worldwide gearing ratio
- Retain an arm's length debt test as a substitute test which will apply only to an entity's external (third party) debt, disallowing deductions for related party debt under this test

Denying deductions for payments made on or after 1 July 2023 relating to intangibles held in low- or no-tax jurisdictions

The Government will introduce an anti-avoidance rule to prevent significant global entities (entities with global revenue of at least $1b) from claiming tax deductions for payments made directly or indirectly to related parties in relation to intangibles held in low- or no-tax jurisdictions.

For the purposes of this measure, a low- or no-tax jurisdiction is a jurisdiction with:
- a tax rate of less than 15 per cent
- a tax preferential patent box regime without sufficient economic substance.

Greater tax transparency

The Government will introduce reporting requirements for relevant companies to enhance the tax information they disclose to the public, for income years commencing from 1 July 2023.

The Government will require:

- Large multinationals, defined as significant global entities, to prepare for public release of certain tax information on a country by country (CbC) basis and a statement on their approach to taxation, for disclosure by the ATO
- Australian public companies (listed and unlisted) to disclose information on the number of subsidiaries and their country of tax domicile
- Tenderers for Australian Government contracts worth more than $200,000 to disclose their country of tax domicile (by supplying their ultimate head entity's country of tax residence)

CORPORATE TAX

COVID-19 grants treated as NANE

The Government has elected to make certain COVID-19 business grants made prior to 30 June 2022, non-assessable, non-exempt income (NANE) for tax purposes. This means that eligible businesses will be exempt from paying tax on the grants. This is subject to eligibility and dependent on the type of certain state and territory business grants. The tax treatment is also only provided in exceptional circumstances, such as the severe economic consequences facing businesses during the COVID-19 pandemic. The state and territory COVID-19 grant programs eligible for the NANE treatment currently declared include several grant programs from Victoria and ACT.

Digital Currencies

The Government will introduce additional legislation to clarify that digital currencies (such as bitcoin) will continue to not be considered foreign currencies for Australian income tax purposes. Broadly, this will mean that digital currencies will continue to be treated as capital gains tax assets where they are held as investments. This measure will be backdated to income years beginning 1 July 2021. The measure provides clarity after the government of El Salvador adopted Bitcoin as legal tender. It is noted that this measure excludes digital currencies issued by or under the authority of a government agency.

Depreciation of intangibles

The Government has announced they will not proceed with the measure to allow taxpayers to self-assess the tax effective lives of intangible depreciating assets that they start to hold on or after 1 July 2023 which was first announced in the 2021-22 Federal Budget. The tax effective lives of intangible assets will continue to be set by statute.

Extend ATO Compliance Programs – Tax Avoidance Taskforce, Shadow Economy Program, Personal Income Taxation Compliance Program

The Government is providing additional funding to extend both the Tax Avoidance Taskforce and Personal Income Taxation Compliance Program. The ATO Tax Avoidance Taskforce's funding will increase by $200m per year for the next four years from 1 July 2022, and its operation extended by one further year from 1 July 2025. This extension is expected to support the ATO in cracking down on new tax risk areas identified in multinational enterprises and large public and private businesses. The measure is estimated to increase receipts by $2.8b over the next 4 years from 2022-23 with a cost to the Government of $1.1b.

The Personal Income Taxation Compliance program will receive $80.3m and be extended for two years from 1 July 2023 with a focus on key areas of non-compliance such as overclaiming of deductions and incorrect reporting of income. The funding is expected to help the ATO modernise its guidance products and improve its compliance activities with taxpayers.

The Shadow Economy Program will be extended for a further three years from 1 July 2023 to allow the ATO to continue targeting shadow economic activity, protect revenue and support the businesses that are following the rules.

Improving the integrity of off-market share buy-back

Effective from 7.30pm AEDT 25 October 2022 the Government will now align the tax treatment of off-market share buy-backs undertaken by listed public companies with the treatment of on-market share buy-backs.

Commonwealth Penalty Unit update

The Commonwealth penalty unit will increase from $222 to $275 from 1 January 2023. This amount is indexed every 3 years in line with CPI, with the next indexation on 1 July 2023. This increase applies to offences committed after the relevant legislative amendment comes into force.

PERSONAL TAX

The Government did not announce any changes to personal tax rates or the proposed **Stage 3 tax** changes which will commence from 1 July 2024.

Under the Stage 3 tax changes, the 32.5 per cent marginal tax rate will be cut to 30 per cent for taxable income between $45,000 and $200,000 and the 37 per cent tax bracket will be entirely abolished.

The budget did not announce any extension of the **low and middle income tax offset** which has now ceased and been replaced by the **low income tax offset** (LITO).

SUPERANNUATION

The Government has not applied any further pressure on retirees, leaving the current superannuation tax rate and current contribution caps unchanged.

There are some further measures which I would have liked to have seen in regard to simplifying the superannuation system, such as the removal of various superannuation caps to just one cap. This would take the confusion out of implementing retirees superannuation strategies, as well as allowing for more affordable strategy advise without the need for various cap calculations currently required.

Year-on-year, tax receipts from superannuation funds are expected to drop sharply in FY23 by 52.5 per cent to $12.6b. Utilisation of franking credits made available through the payment of a significant in-specie dividend, coupled with recent off-market share buy-back activity, is the key driver for the revision.

The Government is expanding eligibility for downsizer contributions, reducing the minimum age eligibility from 60 to 55 years of age. This measure will:

- Allow people to make a one-off post-tax contribution to their superannuation of up to $300,000 per person from the proceeds of selling their home, with this amount not counting towards the non-concessional contribution caps.
- Assist in providing available housing for younger families, allowing retirees to downsize their home to better suit their needs, whilst providing more housing stock for younger Australian families
- Gives individuals who are currently unable to make further contributions (such as having superannuation balances in excess of $1.7m) to now have the opportunity to contribute up to $300,000 per person without breaching superannuation contribution caps

The Government has also expanded the exemption of home sale proceeds from pension asset testing from 12 to 24 months to allow pensioners more time to purchase, build or renovate before their pension is affected.

INNOVATION INCENTIVES

Much needed certainty was provided by the Government to business around its continued support for the R&D Tax Incentive. This reflects the importance placed on innovation as a tool to grow the Australian economy and to provide certainty to businesses planning future investment in R&D based projects. The R&D Tax Incentive (R&DTI) is Australia's flagship innovation program to support companies conducting Australian based R&D activities.

Key big ticket innovation centric items flagged in the Federal Budget include:

- The cornerstone announcement of a National Reconstruction Fund which will provide a $15b investment in key national infrastructure and sovereign manufacturing projects. This reinforces the Government's ongoing support of key priority areas including: resources, agriculture, forestry and fisheries sectors; transport; medical science; renewables and low emission technologies; defence capability; and enabling capabilities.
- Industry specific measures including $50.5m to establish the Australian Critical Minerals Research and Development Hub. The body will focus on domestic and international R&D collaboration to address key challenges in the sector, with a focus on Lithium.

Although the Federal Government did not announce any specific changes to the Export Market Development Grant, it was acknowledged that the global economic slowdown coupled with rising inflation will likely have a negative impact on Australian exports. There was also no mention of the opposition's proposed Patent Box scheme which was in place to encourage innovation in the medical and agricultural sectors. The proposed Patent Box legislation lapsed at the dissolution of Parliament prior to the last federal election.

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