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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

CLEAN ENERGY (INCOME TAX RATES AMENDMENTS) BILL 2011
CLEAN ENERGY (TAX LAWS AMENDMENTS) BILL 2011

EXPLANATORY MEMORANDUM

(Circulated by the authority of the
Deputy Prime Minister and Treasurer, the Hon Wayne Swan MP)

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Glossary

The following abbreviations and acronyms are used throughout this combined explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
LITO	low-income tax offset
MLA 1986	<i>Medicare Levy Act 1986</i>
SAPTO	seniors and pensioners tax offset
SATO	senior Australians tax offset
surcharge	Medicare levy surcharge
the mechanism	the Clean Energy Legislative Package, which sets up the carbon pricing mechanism as part of the Government's climate change plan, as set out in <i>Securing a clean energy future: the Australian Government's climate change plan</i> .

General outline and financial impact

The 2011 Clean Energy Legislative Package

The Clean Energy (Income Tax Rates Amendments) Bill 2011 and the Clean Energy (Tax Laws Amendments) Bill 2011 are part of the Clean Energy Legislative Package, which sets up the carbon pricing mechanism (the mechanism) as part of the Government's climate change plan, as set out in *Securing a clean energy future: the Australian Government's climate change plan*.

The full policy context and background to the mechanism is set out in the explanatory memorandum for the Clean Energy Bill 2011. A description of the Bills which will introduce the mechanism is set out below.

Table 1: The Clean Energy Bill 2011 and related Bills

<i>Bill title</i>	<i>Description</i>
Clean Energy Bill 2011	<p>The Clean Energy Bill 2011 creates the mechanism. It sets out the structure of the mechanism and process for its introduction. These include:</p> <ul style="list-style-type: none">• entities and emissions that are covered by the mechanism;• entities' obligations to surrender eligible emissions units;• limits on the number of eligible emissions units that will be issued;• the nature of carbon units;• the allocation of carbon units, including by auction and the issue of free units;• mechanisms to contain costs, including the fixed charge period and price floors and ceilings;• linking to other emissions trading schemes;• assistance for emissions-intensive trade-exposed activities and coal-fired electricity generators;• monitoring, investigation, enforcement and penalties;• administrative review of decisions; and• reviews of aspects of the mechanism over time.

<i>Bill title</i>	<i>Description</i>
Statutory bodies	<p>The Clean Energy Regulator Bill 2011 sets up the <i>Regulator</i>, which is a statutory authority that will administer the mechanism and enforce the law.</p> <p>The responsibilities of the Regulator include:</p> <ul style="list-style-type: none"> • providing education on the mechanism, particularly about the administrative arrangements of the mechanism; • assessing emissions data to determine each entity’s liability; • operating the Australian National Registry of Emissions Units (the Registry); • monitoring, facilitating and enforcing compliance with the mechanism; • allocating units including freely allocated units, fixed charge units and auctioned units; • applying legislative rules to determine if a particular entity is eligible for assistance in the form of units to be allocated administratively, and the number of other units to be allocated; • administering the National Greenhouse and Energy Reporting System, the Renewable Energy Target and the Carbon Farming Initiative; and • accrediting auditors for the Carbon Farming Initiative and National Greenhouse and Energy Reporting System.
	<p>The Climate Change Authority Bill 2011 sets up the <i>Authority</i>, which will be an independent body that provides the Government with expert advice on key aspects of the mechanism and the Government’s climate change mitigation initiatives.</p> <p>The Government will remain responsible for carbon pricing policy decisions.</p> <p>This Bill also sets up the Land Sector Carbon and Biodiversity Board which will advise on key initiatives in the land sector.</p>
Consequential amendments	<p>The Clean Energy (Consequential Amendments) Bill 2011 makes consequential amendments to ensure:</p> <ul style="list-style-type: none"> • National Greenhouse Energy Reporting System supports the mechanism; • the Registry covers the mechanism and the Carbon Farming Initiative; • the Regulator covers the mechanism, the Carbon Farming Initiative, the Renewable Energy Target and the National Greenhouse and Energy Reporting System; • the Regulator and Authority are set up as statutory agencies and regulated by public accountability and financial management rules; • that emissions units and their trading are covered by laws on financial services;

<i>Bill title</i>	<i>Description</i>
	<ul style="list-style-type: none"> • that activities related to emissions trading are covered by laws on money laundering and fraud; • synthetic greenhouse gases are subject to an equivalent carbon price applied through existing regulation of those substances; • the Regulator can work with other regulatory bodies, including the Australian Securities and Investments Commission, the Australian Competition and Consumer Commission and the Australian Transaction Reports and Analysis Centre; • the taxation treatment of emissions units for the purposes of the goods and services tax and income tax is clear; and • the Conservation Tillage Refundable Tax Offset is established.
Procedural Bills	<p>Those elements of the mechanism which oblige a person to pay money are implemented through separate Bills that comply with the requirements of section 55 of the <i>Constitution</i>.</p> <p>These Bills are the Clean Energy (Unit Shortfall Charge—General) Bill 2011, the Clean Energy (Unit Issue Charge—Fixed Charge) Bill 2011, the Clean Energy (Unit Issue Charge—Auctions) Bill 2011, the Clean Energy (Charges—Excise) Bill 2011, the Clean Energy (Charges—Customs) Bill 2011, the Clean Energy (International Unit Surrender Charge) Bill 2011, the Ozone Protection and Synthetic Greenhouse Gas (Manufacture Levy) Amendment Bill 2011 and the Ozone Protection and Synthetic Greenhouse Gas (Import Levy) Amendment Bill 2011.</p>
Related Bills	<p>Other elements of the Government’s climate change plan are being implemented through other legislation. These are:</p> <ul style="list-style-type: none"> • the Clean Energy (Excise Tariff Legislation Amendment) Bill 2011 and the Clean Energy (Customs Tariff Amendment) Bill 2011, which impose an effective carbon price on aviation and non-transport gaseous fuels through excise and customs tariffs; • the Clean Energy (Fuel Tax Legislation Amendment) Bill 2011, which reduces the business fuel tax credit entitlement of non-exempted industries for their use of liquid and gaseous transport fuels, in order to provide an effective carbon price on business through the fuel tax system; and • the Clean Energy (Household Assistance Amendments) Bill 2011, the Clean Energy (Tax Laws Amendments) Bill 2011 and the Clean Energy (Income Tax Rates Amendments) Bill 2011, which will implement the household assistance measures announced by the Government on 10 July 2011. These Bills amend relevant legislation to provide payment increases for pensioner, allowees and family payment recipients and provide income tax cuts and establish new supplements for low-and middle-income households.

The Bills need to be read in the context, in particular, of the Clean Energy Bill 2011.

Household assistance for a clean energy future

The Clean Energy (Income Tax Rates Amendments) Bill 2011 and the Clean Energy (Tax Laws Amendments) Bill 2011 amend the personal income tax system to deliver tax cuts to households as part of the Government's plan for a clean energy future. Households will also receive assistance through amendments to social security legislation contained in the Clean Energy (Household Assistance Amendments) Bill 2011.

The amendments implement the Government's commitment to assist low- and middle-income households with expected increases in the cost of living arising from the introduction of the *Clean Energy Future Plan*.

Schedule 1 to the Clean Energy (Income Tax Rates Amendment) Bill 2011 amends the *Income Tax Rates Act 1986* to deliver two rounds of tax cuts through increases in the tax-free threshold and corresponding adjustments to statutory tax rates and thresholds. From 1 July 2012, low- and middle-income individuals will receive tax cuts that provide permanent assistance for the impact of the introduction of a fixed carbon price. From 1 July 2015, the Government will deliver further tax cuts to provide assistance for the projected impact of a floating carbon price out to the end of the decade.

Schedule 1 to the Clean Energy (Tax Laws Amendments) Bill 2011 amends the *Income Tax Assessment Act 1936* (ITAA 1936) to adjust the operation of the low-income tax offset, which together with the changes to the tax-free threshold and marginal tax rates, will better align statutory and effective marginal tax rates.

Schedule 2 amends the *Medicare Levy Act 1986* (MLA 1986) and the *A New Tax System (Medicare Levy Surcharge-Fringe Benefits) Act 1999* to increase the Medicare levy low-income thresholds and the associated phase-in limits, to ensure that the Government's personal tax reforms do not result in a person incurring the Medicare levy before they have a tax liability.

Schedule 3 amends the ITAA 1936 to merge the pensioner tax offset with the senior Australians tax offset (SATO), creating a new seniors and pensioners tax offset (SAPTO). This Schedule also amends the MLA 1986 to extend the income threshold at which recipients of the

SATO are exempt from the Medicare levy to all recipients of the new SAPTO.

These amendments will increase the effective tax-free threshold for all individuals from 2012-13, with a further increase in 2015-16.

Date of effect: The amendments in Part 1 of Schedule 1 to the Clean Energy (Income Tax Rates Amendments) Bill 2011, together with the amendments in Part 1 of Schedule 1 and in Schedules 2 and 3 to the Clean Energy (Tax Laws Amendments) Bill 2011, will come into effect on the later of 1 July 2012 or the commencement of the Clean Energy Legislative Package.

The amendments in Part 2 of Schedule 1 to the Clean Energy (Income Tax Rates Amendments) Bill 2011, together with the amendments in Part 2 of Schedule 1 to the Clean Energy (Tax Laws Amendments) Bill 2011, will come into effect on the later of 1 July 2015 or the commencement of the Clean Energy Legislative Package.

Proposal announced: The measures are based on the Government's announcement of its *Clean Energy Future Plan* on 10 July 2011 as set out in *Securing a clean energy future: the Australian Government's climate change plan*.

Financial impact: The financial impact statement is included in the explanatory memorandum for the Clean Energy Bill 2011.

Compliance cost impact: Nil.

Summary of regulation impact statement

Impact: The Regulation Impact Statement (RIS) for the mechanism, entitled *Australia's plan for a clean energy future*, is available at <http://ris.finance.gov.au>. The RIS was prepared by the Department of Climate Change and Energy Efficiency and has been assessed as adequate by the Office of Best Practice Regulation.

Chapter 1

Personal tax rates and low-income tax offset

Outline of chapter

1.1 Schedule 1 to the Clean Energy (Income Tax Rates Amendments) Bill 2011 amends the *Income Tax Rates Act 1986* to raise the tax-free threshold and adjust marginal tax rates from 1 July 2012 and again from 1 July 2015.

1.2 Schedule 1 to the Clean Energy (Tax Laws Amendments) Bill 2011 amends the *Income Tax Assessment Act 1936* (ITAA 1936) to make corresponding adjustment to the low-income tax offset (LITO).

1.3 These amendments will roll most of the LITO into the statutory tax rates and thresholds, making the personal tax system simpler and more transparent and delivering tax cuts for taxpayers earning less than \$80,000 per year.

Context of amendments

1.4 These amendments give effect to the personal income tax cuts announced by the Prime Minister in *Securing a clean energy future: the Australian Government's climate change plan*, on 10 July 2011.

1.5 These amendments improve the simplicity and transparency of the personal income tax system, by increasing the tax-free threshold and rolling most of the LITO into the statutory rates and thresholds.

1.6 Part I of Schedule 7 to the *Income Tax Rates Act 1986* sets out the personal income tax rates and thresholds that apply to the taxable income of individuals who are Australian residents for taxation purposes.

1.7 Section 159N of the ITAA 1936 provides for the LITO for certain low-income taxpayers. The LITO targets tax relief to low- and middle-income individuals by raising their effective tax-free threshold.

Summary of new law

1.8 Part 1 of Schedule 1 to the Clean Energy (Income Tax Rates Amendments) Bill 2011 and Part 1 of Schedule 1 to the Clean Energy (Tax Laws Amendments) Bill 2011 will amend the *Income Tax Rates Act 1986* and the ITAA 1936 respectively so that from 1 July 2012:

- the tax-free threshold will rise from \$6,000 to \$18,200 and the LITO will be reduced from \$1,500 to \$445, meaning low-income earners receive an effective tax-free threshold of \$20,542;
- the first marginal tax rate will be increased from 15 per cent to 19 per cent, and will apply to that part of taxable income that exceeds the tax-free threshold but does not exceed \$37,000, and the withdrawal threshold for the LITO will increase from \$30,000 to \$37,000 aligning the effective marginal tax rate and the statutory rate for taxable incomes within this range; and
- the second marginal tax rate will be increased from 30 per cent to 32.5 per cent, and will apply to that part of taxable income that exceeds \$37,000 but does not exceed \$80,000, and the withdrawal rate for the LITO will be reduced from 4 per cent to 1.5 per cent, with the benefit fully withdrawn at \$66,667, more closely aligning the effective marginal tax rate and statutory rate for taxable income between \$37,000 and \$66,667.

1.9 Part 2 of Schedule 1 to the Clean Energy (Income Tax Rates Amendments) Bill 2011 and Part 2 of Schedule 1 to the Clean Energy (Tax Laws Amendments) Bill 2011 amends the *Income Tax Rates Act 1986* and the ITAA 1936 respectively so that from 1 July 2015:

- the tax-free threshold will increase from \$18,200 to \$19,400 and the LITO will be reduced from \$1,500 to \$445, meaning low-income earners receive an effective tax-free threshold of \$20,979; and
- the second marginal tax rate will increase from 32.5 per cent to 33 per cent, and will apply to that part of taxable income that exceeds \$37,000 but does not exceed \$80,000, and the withdrawal rate for the LITO will be reduced from 1.5 per cent to 1 per cent, with the benefit fully withdrawn at \$67,000.

Detailed explanation of new law

Clean Energy (Income Tax Rates Amendments) Bill 2011

1.10 The amendments to the *Income Tax Rates Act 1986*, together with changes to the LITO, deliver tax cuts to low- and middle-income earners and better align statutory and effective marginal tax rates. The personal income tax rates and thresholds for taxpayers are summarised for resident taxpayers in the table below:

<i>Personal income tax rates and thresholds</i>						
	<i>2011-12</i>		<i>2012-13</i>		<i>2015-16</i>	
	<i>Threshold</i>	<i>Rate</i>	<i>Threshold</i>	<i>Rate</i>	<i>Threshold</i>	<i>Rate</i>
1 st rate	\$6,001	15.0%	\$18,201	19.0%	\$19,401	19.0%
2 nd rate	\$37,001	30.0%	\$37,001	32.5%	\$37,001	33.0%
3 rd rate	\$80,001	37.0%	\$80,001	37.0%	\$80,001	37.0%
4 th rate	\$180,001	45.0%	\$180,001	45.0%	\$180,001	45.0%

1.11 From 1 July 2012, the ‘tax-free threshold’ will be defined at \$18,200 in subsection 3(1), and the first two marginal tax rates in Part I of Schedule 7 will be increased to 19 per cent and 32.5 per cent. [*Schedule 1, items 1 and 3 to 5 of the Clean Energy (Income Tax Rates Amendments) Bill 2011*]

1.12 From 1 July 2015, the ‘tax-free threshold’ will be defined at \$19,400 in subsection 3(1), and the second marginal tax rate in Part I of Schedule 7 will be increased to 33 per cent. [*Schedule 1, items 7 and 8 of the Clean Energy (Income Tax Rates Amendments) Bill 2011*]

1.13 From 1 July 2012, the arrangements to pro-rate the statutory tax-free threshold for individuals and trustees who are residents for taxation purposes for part of the year in subsections 20(1) and (2) will be amended to ensure they receive appropriate assistance for the impact of a carbon price through the personal tax system.

1.14 From 1 July 2012 part-year residents and trustees will be able to access a tax-free threshold of at least \$13,464. Their access to the remaining \$4,736 of the full tax-free threshold will be pro-rated.

1.15 From 1 July 2015 part-year residents and trustees will be able to access a tax-free threshold of at least \$14,664. Their access to the remaining \$4,736 of the full tax-free threshold will be pro-rated. [*Schedule 1, item 2 of the Clean Energy (Income Tax Rates Amendments) Bill 2011*]

Clean Energy (Tax Laws Amendments) Bill 2011

1.16 The amendments to section 159N of the ITAA 1936, which sets out the arrangements for the LITO, are summarised in the table below:

<i>Low income tax offset</i>			
	<i>2011-12</i>	<i>From 1 July 2012</i>	<i>From 1 July 2015</i>
Amount	\$1,500	\$445	\$300
Lower withdrawal limit	\$30,000	\$37,000	\$37,000
Upper withdrawal limit	\$67,500	\$66,667	\$67,000
Withdrawal rate	4.0%	1.5%	1.0%

1.17 From 1 July 2012, individuals will be entitled to receive the LITO if their taxable income is below \$66,667. The maximum value of the LITO will be reduced to \$445 and it will be phased out at the rate of 1.5 cents for every dollar of taxable income over \$37,000. *[Schedule 1, items 1 and 2 of the Clean Energy (Tax Laws Amendments) Bill 2011]*

1.18 From 1 July 2015, individuals will be entitled to receive the LITO if their taxable income is below \$67,000. The maximum value of the LITO will be reduced to \$300 and it will be phased out at the rate of 1 cent for every dollar of taxable income over \$37,000. *[Schedule 1, items 4 and 5 of the Clean Energy (Tax Laws Amendments) Bill 2011]*

Application and transitional provisions

Clean Energy (Income Tax Rates Amendments) Bill 2011

1.19 The amendments in Part 1 of Schedule 1 apply to assessments for the 2012-13 year of income and later years of income. *[Schedule 1, item 6 of the Clean Energy (Income Tax Rates Amendments) Bill 2011]*

1.20 The amendments in Part 2 of Schedule 1 apply to assessments for the 2015-16 year of income and later years of income. *[Schedule 1, item 9 of the Clean Energy (Income Tax Rates Amendments) Bill 2011]*

Clean Energy (Tax Laws Amendments) Bill 2011

1.21 The amendments in Part 1 of Schedule 1 apply to assessments for the 2012-13 year of income and later years of income. *[Schedule 1, item 3 of the Clean Energy (Tax Laws Amendments) Bill 2011]*

1.22 The amendments in Part 2 of Schedule 1 apply to assessments for the 2015-16 year of income and later years of income. [*Schedule 1, item 6 of the Clean Energy (Tax Laws Amendments) Bill 2011*]

Chapter 2

Medicare levy low-income thresholds and Medicare levy surcharge

Outline of chapter

2.1 Schedule 2 to the Clean Energy (Tax Laws Amendments) Bill 2011 amends the *Medicare Levy Act 1986* (MLA 1986) and the *A New Tax System (Medicare Levy Surcharge-Fringe Benefits) Act 1999* to increase the Medicare levy and the Medicare levy surcharge low-income threshold amounts (threshold amounts) at which individuals are exempt from paying the Medicare levy. This Schedule also increases the phase-in limits as a result of the increased thresholds.

Context of amendments

2.2 These amendments give effect to the personal income tax cuts that will assist households for the introduction of a carbon price, announced by the Prime Minister in *Securing a clean energy future: the Australian Government's climate change plan*, on 10 July 2011. The amendments ensure that individuals do not have a Medicare levy liability where they face no income tax liability.

Medicare levy low-income thresholds

2.3 Subsections 7(1) and 8(1) of the MLA 1986 provide that no Medicare levy is payable by low-income individuals and families whose taxable income or combined family taxable income does not exceed stated threshold amounts.

2.4 Pursuant to subsection 7(2), the Medicare levy applies at a reduced rate to taxpayers with taxable incomes above the threshold amount but no more than the 'phase-in limit' specified in subsection 3(1). The rate of the Medicare levy payable in these circumstances is limited to 10 per cent of the excess income over the threshold amount.

2.5 Subsections 8(2) to (4) provide for a reduced Medicare levy to be paid by individuals with a spouse and/or dependants if the individual's family income exceeds the 'family income threshold' prescribed in subsection 8(5) or, for individuals who are entitled for the year of income

to a rebate under section 160AAAA of the *Income Tax Assessment Act 1936* (ITAA 1936), the relevant provision is subsection 8(7).

Medicare levy surcharge low-income threshold

2.6 The Medicare levy surcharge (surcharge) applies on taxable income, including any amount on which family trust distribution tax has been paid, in certain cases where taxpayers do not have appropriate private patient hospital cover pursuant to sections 8B to 8G of the MLA 1986. The surcharge also applies on reportable fringe benefits in certain cases where taxpayers do not have appropriate private patient hospital cover pursuant to sections 12 to 16 of the *A New Tax System (Medicare Levy Surcharge — Fringe Benefits) Act 1999*.

2.7 A taxpayer will not be required to pay the surcharge where the total of their ‘income for surcharge purposes’ does not exceed the individual’s low-income threshold amount. ‘Income for surcharge purposes’ is defined in section 995-1 of the *Income Tax Assessment Act 1997*. Unlike the Medicare levy, there is no shading-in of the surcharge above the threshold amount.

Summary of new law

2.8 Schedule 2 amends:

- subsections 3(1) and 8(7) of the MLA 1986 to raise the threshold amounts and phase-in limits at which individuals are liable to pay an amount of the Medicare levy;
- paragraphs 8D(3)(c) and 8G(2)(c) and subparagraphs 8D(4)(a)(ii) and 8G(3)(a)(ii) of the MLA 1986 to raise the threshold below which a family member is not required to pay the surcharge on taxable income (including amounts on which family trust distribution tax has been paid); and
- paragraphs 15(1)(c) and 16(2)(c) of the *A New Tax System (Medicare Levy Surcharge-Fringe Benefits) Act 1999* to raise the threshold below which a family member is not required to pay the surcharge on reportable fringe benefits.

Detailed explanation of new law

Amendments to the *Medicare Levy Act 1986*

Low-income thresholds

2.9 Schedule 2 increases the low-income thresholds at which individuals are exempt from paying the Medicare levy. These increases ensure that individuals do not have a Medicare levy liability where they face no income tax liability, taking into account the increase in effective tax-free thresholds that result from the tax cuts described in Chapter 1 of this explanatory memorandum.

2.10 The low-income threshold for individuals entitled to an offset under section 160AAAA of the ITAA 1936 is increased from \$30,685 to \$32,279. As a result of amendments described in Chapter 3 of this explanatory memorandum, this threshold will apply to both seniors and pensioners entitled to the new seniors and pensioners tax offset (SAPTO). *[Schedule 2, item 4]*

2.11 The low-income threshold amount for a single individual with no dependants is increased from \$18,839 to \$20,542. *[Schedule 2, item 5]*

2.12 The family income threshold for individuals with a spouse and/or dependants who are entitled to an offset under section 160AAAA of the ITAA 1936, is increased from \$44,500 to \$46,000. This threshold will apply for seniors and pensioners eligible for the SAPTO as a result of amendments described in Chapter 3. *[Schedule 2, item 6]*

Phase-in limit

2.13 The phase-in limit for individuals contained in paragraph (c) of the definition of 'phase-in limit' in subsection 3(1) of the MLA 1986 is increased from \$22,163 to \$24,167. *[Schedule 2, item 3]*

2.14 The phase-in limit for recipients of the offset under section 160AAAA of the ITAA 1936 is increased from \$36,100 to \$37,975. As a result of amendments described in Chapter 3, this phase-in limit will apply to all recipients of the SAPTO. *[Schedule 2, item 2]*

Medicare levy surcharge low-income threshold

2.15 Schedule 2 amends references to the individual low-income threshold amount of '\$18,839' in the Medicare levy surcharge provisions in sections 8D and 8G of the MLA 1986, to '\$20,542'. As a result, taxpayers with income for surcharge purposes below \$20,542 will not be liable to pay the Medicare levy surcharge on any taxable income and

amount subject to family trust distribution tax they have received in the income year. *[Schedule 2, items 7 to 10]*

Amendment to the *A New Tax System (Medicare Levy Surcharge-Fringe Benefits) Act 1999*

2.16 Schedule 2 amends references to the individual low-income threshold amount of '\$18,839' in the Medicare levy surcharge provisions in sections 15 and 16 of the *A New Tax System (Medicare Levy Surcharge-Fringe Benefits) Act 1999*, to '\$20,542'. As a result, taxpayers with income for surcharge purposes below \$20,542 will not be liable to pay the Medicare levy surcharge on any reportable fringe benefits income they have. *[Schedule 2, item 1]*

Application and transitional provisions

2.17 The amendments made by Schedule 2 apply for the 2012-13 year of income and later years of income. *[Schedule 2, item 11]*

Chapter 3

Tax rebate for low income aged persons and pensioners

Outline of chapter

3.1 Schedule 3 to the Clean Energy (Tax Laws Amendments) Bill 2011 amends the *Income Tax Assessment Act 1936* (ITAA 1936) to merge the pensioner tax offset into the senior Australians tax offset (SATO). From 1 July 2012, the pensioner tax offset will no longer be available and all individuals previously eligible for the pensioner tax offset will be eligible for the SATO, which will be known as the seniors and pensioners tax offset (SAPTO).

3.2 Schedule 3 also amends the *Medicare Levy Act 1986* (MLA 1986) to reflect the merger of the pensioner tax offset and SATO and makes further minor consequential amendments.

Context of amendments

3.3 These amendments give effect to the personal income tax cuts that will assist households for the introduction of a carbon price, as announced in *Securing a clean energy future: the Australian Government's climate change plan*, on 10 July 2011.

3.4 Section 160AAA of the ITAA 1936 currently provides for a pensioner tax offset and a beneficiary tax offset.

3.5 Subsection 160AAA(2) allows recipients of certain pensions, allowances and benefits under the *Social Security Act 1991* and the *Veterans' Entitlements Act 1986*, which are known as 'rebtable pensions', to receive the pensioner tax offset, which can be used to reduce the amount of income tax they pay. Subsection 160AAA(3) provides for the beneficiary tax offset which is an offset for recipients of particular allowances that fall within the definition of 'rebtable benefit' in subsection 160AAA(1).

3.6 The amount of pensioner tax offset a person is entitled to receive is determined under Division 2 of Part 8 of the *Income Tax Regulations 1936*. The amount varies depending on the person's 'rebate income' and the rate of pension they are receiving. Pursuant to

Regulation 150AE of the *Income Tax Regulations 1936*, unused amounts of the offset can be transferred to a person's spouse if that spouse is entitled to the SATO.

3.7 Section 160AAAA of the ITAA 1936 allows a person qualified for the Age Pension under the *Social Security Act 1991*, who is not in jail for the whole year, to receive a tax offset, known as the SATO, which can be used to reduce the amount of income tax they pay.

3.8 The maximum amounts of SATO that a person can claim are specified in Sub-regulation 150AB(2) of the *Income Tax Regulations 1936*. The maximum amounts are: \$2,230 for a single; \$1,602 for a member of a couple not separated by illness; and \$2,040 for a member of a couple separated by illness. Pursuant to Regulation 150AE of the *Income Tax Regulations 1936*, unused amounts of SATO can be transferred to a person's spouse if that spouse is also entitled to the SATO.

3.9 Taxpayers entitled to an amount of pensioner tax offset or SATO are eligible for an increased income threshold at which they are exempt from paying the Medicare levy or pay a reduced levy.

3.10 Subsection 7(1) of the MLA 1986 provides that an individual is exempt from paying the Medicare levy if their taxable income is less than the 'threshold amount' as defined in subsection 3(1). Subsection 7(2) provides for a phased amount of the Medicare levy to be paid if the individual's taxable income exceeds the 'threshold amount' but not the 'phase-in limit' in subsection 3(1).

Summary of new law

3.11 From 1 July 2012, the pensioner tax offset will no longer be available and all individuals who would otherwise have been eligible for the pensioner tax offset will instead receive the SATO, which will be known as the SAPTO.

3.12 From 1 July 2012, individuals exempt from the Medicare levy up to the income threshold applying to recipients of the pensioner tax offset will be exempt from the Medicare levy up to the income threshold applying to individuals entitled to the SAPTO (being the income threshold that formerly applied to individuals entitled to the SATO).

Detailed explanation of new law

3.13 Schedule 3 inserts a cross-reference to the definition of ‘rebatable benefit’ in subsection 160AAA(1) of the ITAA 1936 into the definitions section in subsection 6(1) of the ITAA 1936. A ‘rebatable benefit’ is any payment specified under subsection 160AAA(1), which includes allowances paid under the *Social Security Act 1991* as well as various other government income support payments. *[Schedule 3, item 1]*

3.14 The heading for section 160AAAA reads ‘Tax rebate for low income aged persons’, reflecting the continued use of the term ‘rebate’ to describe tax offsets in the ITAA 1936. This heading is amended to reflect the expansion in the class of people eligible for the SATO. *[Schedule 3, item 2]*

3.15 Subsection 160AAAA(1) is amended to clarify that a person’s entitlement to the SAPTO is subject to the terms of amended subsection 160AAA(4). Subsection 160AAA(4) deals with situations where a person is eligible for both the SAPTO and beneficiary tax offset in an income year. *[Schedule 3, item 3]*

3.16 Pursuant to new paragraph 160AAAA(2)(c), recipients of ‘social security pensions’ and ‘service pensions’ under the *Social Security Act 1991* and the *Veterans Entitlements Act 1986*, as well as recipients of limited other benefits largely payable to pension recipients, will be eligible for the SAPTO so long as the individual is not in jail for the whole year. This accords with the requirements for the former SATO. *[Schedule 3, items 4 to 6]*

3.17 The payments described in new paragraph 160AAAA(2)(c) would have previously entitled individuals to an amount of pensioner tax offset. As a result of this amendment, only benefits available to individuals fitting the description of pensioner are to entitle the individual to an amount of SAPTO.

3.18 The heading for section 160AAAB reads ‘Tax rebate for low income aged persons — trustees assessed under section 98’. This heading is amended to reflect the expansion of the beneficiaries described in section 160AAAA in respect of whom a trustee may claim an offset under section 160AAAB. *[Schedule 3, item 7]*

3.19 Section 160AAAB allows a trustee liable to be assessed under section 98 of the ITAA 1936 to claim an amount of offset in respect of a beneficiary’s share of the net income of the trust estate if the beneficiary would be eligible for an offset under section 160AAAA.

3.20 Schedule 3 amends subsection 160AAAB(2) to reflect the expansion of the class of individuals eligible for an offset under section 160AAA. *[Schedule 3, items 9 to 11]*

3.21 Subsection 160AAAB(1) is also amended to clarify that a trustee's entitlement to an offset under that section is subject to amended subsection 160AAA(4A). Subsection 160AAA(4A) deals with the situation where a beneficiary is eligible for an amount of beneficiary tax offset in the same year that a trustee is eligible for an amount of offset under section 160AAAB in respect of that beneficiary's share of the net income of a trust estate. *[Schedule 3, item 8]*

3.22 Current section 160AAA allows a person who receives certain social security payments and benefits to receive either the pensioner tax offset or the beneficiary tax offset.

3.23 The heading for section 160AAA reads 'Rebate in respect of certain pensions, benefits etc'. This heading is amended to reflect the abolition of the pensioner tax offset from section 160AAA. *[Schedule 3, item 12]*

3.24 Subsection 160AAA(2) and the definition of 'rebtable pension' in subsection 160AAA(1) are repealed to give effect to the abolition of the pensioner tax offset. The definition of 'rebtable pension' formerly described the forms of pension, allowance or benefit entitling an individual to an amount of pensioner tax offset. *[Schedule 3, items 13 and 14]*

3.25 Subsection 160AAA(4) is amended so that a person entitled to both the SAPTO and the beneficiary tax offset in an income year is able to claim one, but not both, of the offsets if they are of the same value, or the offset of the greater value if they are not the same. *[Schedule 3, item 15]*

3.26 Former subsection 160AAA(4A) is repealed and a new subsection inserted in its place. New subsection 160AAA(4A) provides that an individual is not entitled to an amount of beneficiary tax offset if they are the beneficiary of a trust whose trustee is entitled to an offset under section 160AAAB and the amount of that offset is the same or greater than the amount of beneficiary tax offset. *[Schedule 3, item 16]*

3.27 If the offsets are of different value, then the trustee or beneficiary, as appropriate, may claim the offset of greater value.

3.28 Schedule 3 amends the definitions of 'phase-in limit' and 'threshold amount' in the MLA 1986 to remove the separate references to specific amounts for recipients of the pensioner tax offset. *[Schedule 3, items 22 and 23]*

3.29 The merger of the pensioner tax offset into the SATO means that a specific Medicare levy phase-in limit for recipients of the pensioner tax offset, for taxable income above which a person is liable to pay the full 1.5 per cent Medicare levy on their entire taxable income, is no longer relevant. Similarly, the specific threshold amount for recipients of the pensioner tax offset, for taxable income below which a person is exempt from paying the Medicare levy, is also no longer relevant.

Application and transitional provisions

3.30 The amendments made by this Schedule apply to the 2012-13 income year and later income years. *[Schedule 3, item 24]*

Consequential amendments

3.31 Section 13-1 of the *Income Tax Assessment Act 1997* provides a list of tax offsets available. Section 13-1 is amended to account for the merger of the pensioner tax offset into the SATO. *[Schedule 3, items 17 to 19]*

3.32 The table in subsection 63-10(1) provides the order which tax offsets are applied against a person's income tax liability. Subsection 63-10(1) is amended to account for the merger of the pensioner tax offset into the SATO. *[Schedule 3, items 20 and 21]*

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