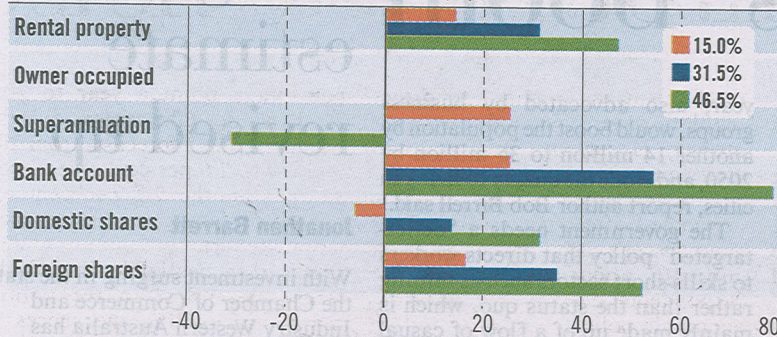


## Not enough

Current approach to taxing different investments (%)



Proposed approach to taxing interest

- **From July 2012,** the government will allow a 50% discount on net interest income up to \$500.
- **From July 2013,** the government will allow a 50% discount on net interest income up to \$1000.

### Example

- Renee has \$2500 of gross interest income and \$500 of expenses.
- Her net interest income is \$2000. As this exceeds the cap, the maximum discount of \$500 will apply.
- Instead of taxable interest income of \$2000, Renee now has taxable interest income of \$1500 in July 2013-14.



SOURCE: TREASURY

# Interest incentive falls short

**Anthony Sibillin**

The federal government's 50 per cent tax discount on interest income needs to be five to 10 times higher to induce people to save more, bank and tax experts have warned.

Treasury released a discussion paper last week on the plan to exempt 50 per cent of interest from bank deposits, bonds, debentures and annuities — up to \$500 — in 2012-13, rising to \$1000 in later years.

The discount, announced in last year's budget, was to begin this financial year. But the government pushed it out by a year and halved the amount in the first year to help pay for spending promises to independent MPs last September.

Online bank RaboDirect's general manager, Greg McAweeney, welcomed any measure to reduce the bias in the tax system toward other investments, especially property and shares. But he said the \$1000 cap was a long way short of the substantial tax relief afforded to savers in most other countries. "The level of tax on deposits here will still be too high by global standards."

Mr McAweeney said a cap of at least \$5000 was needed to induce more saving.

Bond specialist FIIG's fixed income research director Justin McCarthy reckoned a \$10,000 cap would be necessary to change investors' behaviour.

"It is a good first step, but we

would like to see it extended," he said. "We are very glad it includes interest on bonds and debentures and products like that."

Dominic Stevens, chief executive of Challenger, the country's biggest provider of annuities, is also pleased the interest component of annuity payments will attract the tax discount.

"Given the global financial crisis and ongoing volatility, any measure to encourage more secure forms of saving and investment should be applauded," he said.

"We're pleased annuities have been treated the same way as bank deposits, and would welcome a

### Any measure to encourage more secure forms of saving and investment should be applauded.

Dominic Stevens, Challenger

similar approach with the deposit guarantee scheme so as to achieve competitive neutrality amongst [Australia Prudential and Regulatory Authority] regulated entities."

The 2008 tax review by former Treasury boss Ken Henry recommended a 40 per cent income discount apply to all investments.

The review noted interest income received the "least favourable tax treatment" of all asset classes.

"The entire return, including

inflationary gains, is included annually in taxable income, generating an effective marginal tax rate on the real return greater than the statutory marginal personal tax," the Henry report says.

In contrast, shares and properties benefit from the capital gains tax discount, domestic shares from dividend imputation and debt-funded properties from negative gearing.

In its submission to the Henry review, the Australian Bankers' Association preferred a flat 15 per cent tax on interest income.

"Our basic position was about equity with other investments," ABA policy director Tony Burke said.

One element of the proposal the industry is expected to challenge is the exclusion of fees and other expenses. Instead, the discount will apply to "net" interest income only.

The paper claims this will "minimise the burden" on trusts and partnerships that, unlike companies, associations and superannuation funds, will get the discount.

"While trusts and partnerships will likely have to alter existing reporting or distribution statements . . . a gross interest income discount would likely result in additional complexity and compliance costs as any net interest income would need to be further separated between gross interest income and their related expenses," the paper says.

Mining tax distorting, page 42 ■  
Congestion reform call, page 55 ■