more give, less take

nab

Federal Budget 2015

What the Federal Budget means for Small Business.

About Small Business

NAB is Australia's leading business bank. With over 200 Business Banking Centres and offices across the country, our team comprises of more than 4,000 business bankers nationally. NAB provides the full suite of commercial services to our business customers, ranging from very small businesses through to Australia's largest corporations.

NAB takes a long-term view on the businesses we support and take the time to understand your business and the challenges and opportunities you face. We lend to more Australian business than any other bank and believe in the potential of our customers and communities.

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Federal Budget overview

Our economists' view

Alan Oster, Group Chief Economist, NAB

The focus of the 2015 Federal Budget is very different from last year. Given the political problems of last year's budget, the focus has been on attempting to make this Budget as politically saleable as possible. Also, unlike last year, the 2015 Budget is relatively neutral in its impact on the broader economy. Essentially, new expenditures have been broadly offset by savings.

More than any budget in recent memory, most of the key changes were pre-announced/leaked – again to emphasise the 'no surprises' focus. Consequently, the key spends include a $5.5bn small business package (really micro business, that is turnover of less than $2m per annum). This included tax cuts and, more importantly, a 5% tax discount (up to $1,000) to other tax payments, immediate write-offs of new assets up to $20,000, tax advantages for crowd funding and GST exemptions to SME electronic purchases. Elsewhere there is $3.5bn (over five years) spending on childcare incentives (linked to stalled family tax benefits savings); a new infrastructure fund for Northern Australia ($800m); extra incentives for employment of older Australians; drought spending ($330m); border protection/terrorism prevention ($500m); a payment to offset Western Australia's GST issues ($500m); extra spending on the Pharmaceutical Benefits Scheme ($1.6bn) and the reversal of last year's doctor rebate savings.

The savings were equally well flagged. These include a new law on cross-border profit shifting: GST on intangible/services (The 'Netflix tax'); pension savings by lowering the non-home asset threshold to $800,000 ($2.4bn); tightening of the paid parental schemes (anti-double dipping between private and public schemes); the withdrawal of money for Melbourne's East West Link ($1.5bn); and further public service efficiency dividends.

As set out in the section on the medium term fiscal outlook, the Budget really is a combination of redirected policy spending broadly offset by substantial increases in revenue to GDP – bracket creep. Outlays broadly grow in line with GDP, which is better than the previous upward trend. Also, the economic impact of the Budget on the economy is relatively neutral.

Broadly, the Government's forecasts are very similar to NAB's, so we see the projections as credible. Of course to the extent we have all overestimated growth – especially in a low wage growth and falling commodity price world – the Budget remains open to the disappointments (especially on the revenue line) that we have seen in recent years. But with a credible set of forecasts (and a deliberately conservative iron ore price assumption – Treasury's $US48 vis-à-vis NAB's $US60 per tonne) the rating agencies should be relatively satisfied. Equally we would not expect the very negative reaction of consumers to this year's Budget. That said, we would not really expect much of a kick to business confidence, outside of micro business.

Of course the Budget is not the complete current fiscal story. There is still the Tax White Paper to come. The Budget had little on big tax and superannuation questions. Also, there is still the debate about what happens to Government's removal of $80bn in state funding for health and education in the out-years. And finally, despite the Government's best efforts, what happens in the ensuing political process is unknowable.

Fiscal Outcome

The underlying cash deficit for 2014-15 is estimated at $41.1bn and $35bn in 2015-16 (or 2.1% of GDP and below market expectations – but near NAB's). The projected deficit then moves down to $14.4bn in 2017-18 (0.8% of GDP) with an eventual return to surplus in 2019-20. Basically the reduction in the deficit is driven by returning revenues, which rise from 23.9% of GDP in 2014-15 to 25.7% in 2017-18 (accruals basis). Outlays move from 26.1% to 26% of GDP in the same period.

Economic Outlook

As noted above, there is little fundamental difference between Treasury's and NAB's economic outlook. At the margin, we are slightly less optimistic in the near term (NAB 2.3% Treasury 2.5% in 2014-15) but slightly more optimistic in 2015-16 (NAB 2.9% Treasury 2.75%). An interesting difference here is our slightly more pessimistic view on business investment. That said, the RBA is more pessimistic on 2015-16 growth than either Treasury or NAB. At the margin, Treasury has a slightly higher unemployment rate in year average terms in 2015-16 (NAB 6.25% Treasury 6.5%). Finally, on the critical nominal GDP forecasts (for Budget deficit forecasting) there is little difference between NAB and the Treasury (both around 1.5% and 3.5% in the next financial year).

Financial Markets

There was modest but nonetheless positive market reaction to the Budget. The $A has pushed 30bps higher towards 0.7990, although it was trading higher before the Budget's release. Bond futures improved 2-3 bps (i.e. yields lower), presumably because the debt program is a little less than expected and the major ratings agencies have been quick to say the Budget doesn't pose any immediate threat to the AAA rating.

For more detailed analysis from NAB Group Economics, please visit **nab.com.au/fedbudget**

Key initiatives:

- A 1.5% company tax cut for about 780,000 small firms with annual turnover of less than $2m. Lowest level in 50 years. Beginning 1 July 2015.
- Keeping the maximum rate of franking credits at 30% so the cut in company tax for small firms does not have consequences for dividend recipients.
- A 5% discount on the tax payable by unincorporated businesses (sole traders, partnerships or trusts) on their business income. The discount is capped at $1,000 per individual in an income year, delivered as a tax offset. It only applies to businesses with annual turnover of less than $2m.
- An expanded accelerated depreciation allowance giving small businesses (with annual turnover of less than $2m) an immediate tax deduction on individual assets costing less than $20,000, (the previous limit was $1,000). The assets must be acquired and installed by the end of June 2017.
- Small businesses that keep the same owners but might benefit from changing their legal form will be allowed to do so from 2016-17 without triggering capital gains tax. Instead, they can get rollover relief on the capital gains tax.
- Business start-ups will be allowed to immediately deduct professional expenses associated with start-up fees (legal, accounting etc) from the 2015-16 income year.
- Funding for streamlined procedures involving a single, online portal for business registration and reduction in the number of business identifiers to cut red tape.
- Funding for ASIC to develop new rules that can support crowd funding.

NAB's view

The Government has said repeatedly that small business is the lifeblood of our economy, so it should be no surprise that a $5.5bn small business package forms the centrepiece of the 2015 Budget. At NAB, we have confidence in the future of Australian business, and the small business measures in this budget will help to build confidence and support business to invest, hire and grow.

The Government has focused its tax cuts on small business which represent around 95% of all businesses. That means, after excluding loss-making firms, about three-quarters of all businesses could benefit from the reform.

The scale of the tax cuts is not large – 1.5% for companies with an annual turnover of less than $2m and a 5% tax discount for unincorporated businesses capped at $1,000 per individual. But the last cut in company tax was as long ago as 2001 and these reductions are being presented as the first step in a journey toward lower company taxes.

The difficult budget position limits the Government's room to manoeuvre so far as tax cuts are concerned. Still, even with today's quite limited reductions, and despite not accepting business lobbies' request for an increase in the ATO's definition of small business, sizeable sums of money are involved. The total cost of the tax cuts out to 2018-19 is $3.3bn and toward the end of that period the annual cost will be running at about $1bn. Given that small business accounts for $7.4bn of the total $64bn paid in company tax and the costs to revenue of providing this targeted tax cut are high, an across-the-board company tax cut would involve much larger sums than those in the Budget. The cuts are, however, a good start in a difficult budgetary climate.

The accelerated depreciation scheme for small business is the other big ticket measure and it is clearly intended to lift Australia's performance on business investment growth. By putting a sunset date of June 2017 for having assets acquired and installed ready for use, the Government's hope is that capital spending will be pulled forward to help start a virtuous circle of business growth.

Rather than using an investment allowance to encourage spending, the Government has opted for a form of accelerated depreciation that involves a very substantial rise in the threshold sum for immediate write-off by small business. The Henry tax review suggested a $10,000 threshold and there was a $6,500 limit in place until 2014 when it was cut to $1,000. The Budget outcome is a $20,000 threshold, exceeding expectations, which ought to encourage more investment spending in the small business sector.

As with the tax cuts, this reform entails substantial amounts of foregone revenue with annual costs of $850m by 2017-18 and total revenue losses of almost $2bn between May 2015 and 2017-18.

Apart from the costly tax cuts and accelerated depreciation, the rest of the Budget measures are generally valuable, lower profile and much less costly reforms. Improving the regulations to make crowd funding easier, giving rollover relief on capital gains tax to small start-ups changing their legal form, making it less complicated to register a small business and allowing the immediate deduction of professional expenses when starting up a business are all good outcomes for small business.

Several areas that business groups identified as priorities in the lead up to the Budget were not addressed. Notably, the more symmetrical tax treatment of revenue losses (which would favour loss carry-back instead of carry-forward), an increase in the ATO definition of small business above $2m (which would allow more firms to access the tax concessions on capital gains and depreciation that are specific to small business) and the concessional taxation of new R&D through a "patent box" regime.

We can expect business to continue pressing for these changes as the Government progresses the Tax White Paper it plans to take to the 2016 general election. Administering FBT is always a hot issue with small business and, apart from extending the FBT exemption for work-related portable electronic devices, the Budget seems to have largely left that matter to be addressed by the White Paper.

Industry comment

As would be expected, the Budget measures for small business have been welcomed by business groups. The Australian Chamber of Commerce and Industry (ACCI) says the budget "turbocharges small businesses to grow, invest and hire" with its range of small business friendly measures and they ask the Opposition to support them. The ACCI is particularly pleased that small, unincorporated businesses were not forgotten in the tax cuts and believes that the Budget should help restore confidence among small businesses, "the engine room of the Australian economy".

The Council of Small Business of Australia (COSBOA) is impressed with what it calls a 'ground breaking Budget' that it says has delivered on the Government's promises to small business. It is particularly pleased with the $20,000 threshold for immediate write-off by small business and the 5% tax discount for unincorporated small business.

The Australian Industry Group thinks that the budget makes "a good start in improving incentives to invest and create jobs", especially for small business, and it particularly welcomes the increased threshold for assets that can be immediately written off. It stresses that more needs to be done and says that an across-the-board tax business cut (that is, one not just confined to small business) has to be a high priority.

The Business Council of Australia (BCA) describes the Budget as "sound, sensible and thoughtful". It thinks that the two-tier company tax rate (28.5% for firms with turnover under $2m, 30% for those above) is certainly not ideal but draws comfort from the fact that "the impact of these measures is confined to a small part of the economy". The BCA reiterates that the Government should aim for a lower company tax rate across the board to boost the international competitiveness of Australia in the attraction of global capital but only when the budget allows it.

The Institute of Public Accountants has long been calling for policies that boost the productivity of small business and it believes the Government has delivered. It outlines a series of budget announcements that should please small business owners.

The CPA was critical of the government for not going further toward addressing medium term economic problems in the budget but it saw the small business measures as its "shining light" – especially the tax cuts and accelerated depreciation. An across the board tax cut and more focus on R & D were the CPA's priorities.

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