Your Money
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Carbon Tax – What it Means for Investors

The carbon tax is something that very few are in favour of, but it is the Government's preferred method for changing our behaviour. Time will tell whether the government is successful in meeting their objective of reducing emissions of 5% by 2020 and 20% by 2050 by providing incentives to the big business to find creative ways to cut their emissions.

What does this mean to the consumer?

- The tax is forecast to increase electricity prices by 10%, and gas prices by 9%, but a general increase in inflation of just 0.7%. By contrast, the Howard government's GST added an initial 3.1% to inflation in 2000-01 and another 1.9% in 2001-02.

- The Reserve Bank (RBA) will set out to factor the impact of the carbon tax on inflation when setting interest rates. Interest rates would only rise if the RBA felt that the carbon tax was raising inflationary expectations or changing wage setting behaviour.

- Average household costs are expected to increase by about $9.90 per week and higher income earners effectively receive no compensation to cover the higher costs.

- Tax cuts will be provided to low and middle income earners by higher social security payments (+1.7%) and a tripling of the tax free threshold from $6,000 to $18,200 from 1 July 2012 and $19,400 from 1 July 2015. Nine out of 10 households will receive some assistance.

- There will also be tax rate increases from 1 July 2012. The two lowest marginal income tax rates will rise from 15% to 19%, and from 30% to 32.5%, respectively.

Impact on Investment Strategies

- The carbon tax will have a profound impact on our economy. There will be material price changes in many products, and long term structural change in the economy that will see traditional industries – like coal-fired power generation – shrink and others, like various forms of renewable energy, rise.

- The market has been anticipating the carbon tax for some time and most major aspects had been leaked in advance.

- The biggest surprise was the increase in the tax free threshold to $18,200. This will free 1 million Australians from completing annual tax returns and picks up on the Henry Tax review recommendation to encourage the lower income earners to move from welfare to work.

- When allocating income from a family trust each year, the higher tax free threshold may create opportunities to stream income to particular beneficiaries. For example, self-funded retirees who receive a pension and have little taxable income could receive a distribution from the trust of up to $18,200 each year tax free.

- From 1 July 2012 when the 15% marginal tax rate increases to 19%, this will provide additional incentive for low income workers to contribute more of their salary directly into superannuation, where it will be taxed at 15%.

So whilst there are opportunities for some, more than likely the report card on the success of this policy will be written by Generation Y in 2050.

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