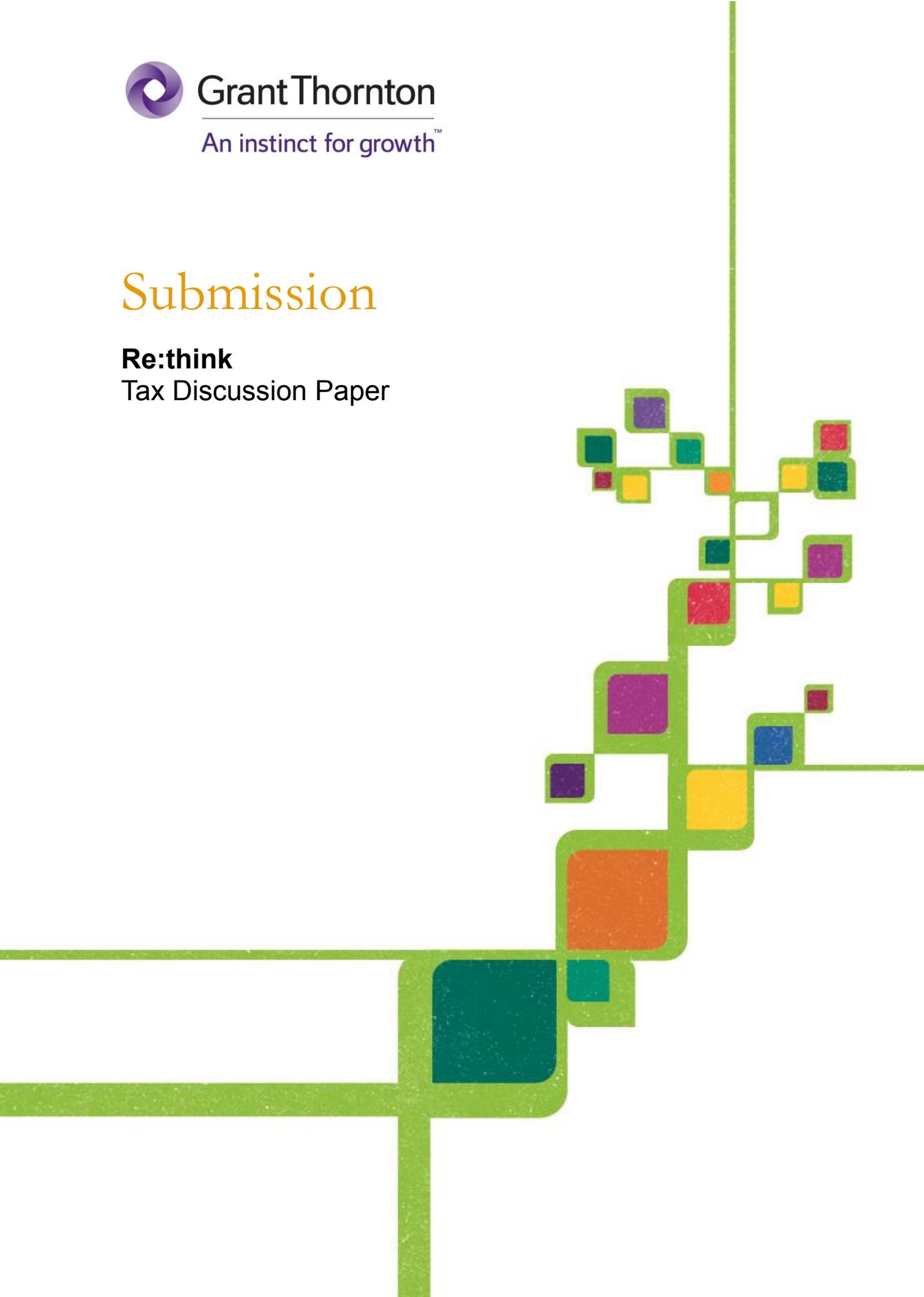


# Submission

**Re:think**  
Tax Discussion Paper



Tax White Paper Task Force  
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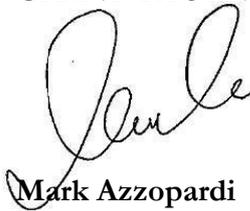
Dear Sir/Madam

Grant Thornton Australia Limited (Grant Thornton Australia) appreciates the opportunity to provide comments to Treasury on the Re: think Tax Discussion Paper dated March 2015.

Our response in the pages following reflects our position as leading advisers to Australia's mid-sized businesses.

Should you have any queries in relation to these matters please contact me on +61 3 8663 6200.

Yours sincerely  
GRANT THORNTON AUSTRALIA LIMITED



**Mark Azzopardi**  
Managing Partner - National Specialist Tax & National Tax Leader

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# Executive Summary

It is clear that tax reform is long overdue. The message we receive from our clients and industry generally is that they are facing significant challenges with the current business environment, and an administratively cumbersome and unsupportive tax system is adding to those challenges. Their concern is not simply about a reduction in tax rates. Their issues go to such things as excessive red tape, lack of support to business, and inefficient revenue collection.

Grant Thornton is a supporter of Mid-Sized Business (MSB), which make an outsize contribution to the Australian economy. With combined annual turnover in excess of \$1.1 trillion, the MSB sector injects an estimated \$241 billion into the economy annually in wages and salaries. Yet despite their economic heft, they're curiously invisible to government and generally under-supported. While small businesses are rewarded in this budget, we question why similar support was not provided to the MSB.

In listening to our MSB clients Government needs to put in place policy settings to boost investment, confidence and jobs and restore trust in the political process.

At Grant Thornton, we believe this can be achieved by:

- Reduction in the corporate tax rate
- Broadening of the GST base and/or increasing the GST rate and/or removing the GST-free treatment enjoyed by certain goods and services and instead treating these goods and services as input taxed.
- No further reduction in caps for expenditure or rate of tax offsets for R&D
- Rationalisation of the state tax system to eliminate inefficient taxes such as stamp duty and payroll tax
- Increased incentives for Australian businesses looking to export overseas
- Review of individual tax rates with a view to aligning them with those of our Asia Pacific neighbours
- Limiting some of the existing tax concessions in the superannuation system
- Re-introducing the investment allowance regime and extending the small business immediate asset write-off concessions announced in the 2015/16 Federal Budget to all companies
- Providing tax relief for intangible assets

Grant Thornton welcomes the opportunity to provide comments in support of effective tax reform, and set out below our views in a number of areas identified in the discussion paper. We look forward to providing further feedback on the Government's proposals on tax reform.

# Challenges for Australia's tax system

## Discussion questions

*1. Can we address the challenges that our tax system faces by refining our current tax system? Alternatively, is more fundamental change required, and what might this look like?*

As highlighted in the Paper, among the key challenges facing the tax system include:

- the rapid and transformative effect of technology on how business is done. Commentators suggest that the pace of change will only increase.
- the rise of international cross border trade including multinational corporations.
- increased financial deregulation.

The above suggests that the evolution of new business models not yet seen appears likely. As a result refining the current tax system appears likely to provide only a short term fix and risks the tax system being subject to continual 'catch up' refinements. Instead we would favour a more fundamental change to move to a stable, broad and simple consumption based tax such as GST. Later in our responses, we examine this principle in more detail, but highlight this as a means to provide a simpler, more efficient tax system.

Moving towards principles based legislation and/or an accounts based approach for corporates could decrease complexity and reduce compliance costs. i.e. items recognised for tax when/if they are recognised as income under accounting principles.

# Australia's tax system

## Discussion questions

### *3. How important is it to reform taxes to boost economic growth? What trade-offs need to be considered?*

Local industries (e.g. manufacturing, food, beverage and agriculture etc.) should be supported to encourage domestic production and greater export activity, especially in an environment where we will need to accommodate a downturn in the mining industry.

It is crucial that the tax system not be seen as an inhibitor to business which will be looking for productivity gains and international competitiveness. Innovation needs to be supported and rewarded by R&D support, and potential tax breaks for innovation and increased export activity. While this may seem to provide short term challenges on Australia's financial position, we would argue that this trade off will assist in providing a long term gain of sustained economic growth

As discussed later, this will involve trade-off between Federal and State taxing rights and the movement between Direct and Indirect taxes.

### *4. To what extent should reducing complexity be a priority for tax reform?*

In aggregate, Australia's tax system is one of the most complex, with many highly prescriptive rules and piecemeal provisions.

As a result, many taxpayers suffer high compliance costs in fulfilling their tax obligations.

In our view, reducing the inter-related complexity of the Australian tax system and eliminating resultant inefficiencies should be a key focus area when designing tax reform measures.

# Individuals

## Discussion questions

*11. How important is tax as a factor influencing people's decisions to work in other countries?*

The exposure to taxes in high cost jurisdictions can lead to difficulties in attracting and retaining talent, especially in highly skilled roles where global competition is fierce. We would suggest that Australia should review individual income tax rates to be more in line with our competitors in the region, for example Singapore and Hong Kong. Commentators suggest that the pace of change will only increase.

# Savings

## Discussion questions

*22. How appropriate are the tax arrangements for superannuation in terms of their fairness and complexity? How could they be improved?*

We believe that the superannuation system should be robust in securing benefits and promoting growth but should also allow flexibility in terms of investment choice.

Grant Thornton are supportive of some of the incentives within the superannuation system such as the tax deductibility of contributions and the concessional tax rates of 15% and 30% within superannuation funds but we believe that other existing tax concessions, such as the tax exemption on withdrawals for those over 60 years of age, are overly generous and provide too great an incentive for members.

In our view, the tax exemption of earnings in the pension phase should be examined. However, we believe that this should not be undertaken in isolation, but as part of a wider consideration of other measures including the refund of excess franking credits and the taxation of withdrawals from superannuation funds.

Grant Thornton would support the imposition of tax on member withdrawals where the taxable component of the withdrawal exceeds a defined annual threshold, for example, \$200,000.

We do not believe it is appropriate to provide only a partial tax exemption for earnings supporting a pension as this is likely to involve significant compliance costs and would be open to abuse via the use of multiple superannuation accounts.

In our view, the current “use it or lose it” nature of concessional contribution caps may disadvantage private business owners as they direct their excess funds towards reinvesting in and growing their businesses. We would support any measure allowing accumulation of concessional contribution caps over time to enable taxpayers to “recoup” and use any unused concession contribution caps in future years.

Grant Thornton does not support enabling taxpayers to borrow from their superannuation balances to fund private housing, as we believe this would create inflationary pressure on house prices and could allow people to extend themselves beyond appropriate levels.

We believe the existing measures allowing funds to borrow under limited recourse borrowing arrangements should be reviewed to ensure better protection of member benefits. We would support a cap on permitted lending to be facilitated by maximum Loan to Value Ratios (LVRs) to achieve this objective.

# General business tax issues

## Discussion questions

*24. How important is Australia's corporate tax rate in attracting foreign investment? How should Australia respond to the global trend of reduced corporate tax rates?*

Australia's corporate tax rate is a key factor in foreign investment decisions and a driver of economic growth.

Australia's corporate tax rate is currently relatively high compared to many countries in the region, leaving it at a competitive disadvantage when competing for foreign investment.

It is imperative that the corporate tax rate be reduced to enable Australia to compete on a more level playing field for the foreign investment which is key to its economic future. The 2014/15 Federal Budget went some way towards this by reducing the small business company tax rate to 28.5% but we believe this reduction should be extended beyond small business. We also believe that it is desirable to consider an across-the-board further rate reduction.

Grant Thornton believes a corporate tax rate of 25% is appropriate for Australia to stimulate growth and enable it to effectively compete for foreign investment in the Asia Pacific region.

*27. To what extent does the tax treatment of capital assets affect the level or composition of investment? Would alternative approaches be preferable and, if so, why?*

The tax treatment of capital assets has a major impact on the level and composition of investment by mid-sized businesses (MSBs).

The tax attributes of capital assets can be a major determinant for MSBs in their investment decisions as they may be less able to absorb the higher incidences of tax associated with certain capital assets.

We recommend that the investment allowance regime be re-introduced to stimulate capital investment by MSBs. The government should also consider extending the small business immediate tax write-off measures announced in the 2014/15 Federal Budget to MSBs to provide them with a greater incentive to invest in capital assets which should lead to increased efficiencies and growth in the MSB sector.

*29. To what extent does the tax treatment of losses discourage risk-taking and innovation and hinder businesses restructuring? Would alternative approaches be preferable and, if so, why?*

Grant Thornton supports the reintroduction of the Loss carry back provisions. This measure was a clear example of providing targeted support to business at a difficult juncture in their life cycles. Support of this nature will enable Australian companies to more effectively manage the fluctuations of operating in a global economic environment.

*30. How could the current tax treatment of intangible assets be improved?*

A number of other jurisdictions, including the UK, provide some measure of tax relief for intangible assets in recognition of the growth in technology companies and the increasing importance of brand names. In the UK relief applies to companies only and, in broad terms, provides that a company's gains in respect of intangible fixed assets are chargeable to corporation tax as income and its losses obtain tax relief. Moving to unified treatment of intangible assets could increase Australia's international competitiveness and simplify the current differing treatments depending on the type of intangible asset concerned.

*37. Are there other important issues in the business tax system, not covered in this section, which should be considered as part of the tax white paper process?*

We submit that family business is a category which demands special consideration. In March 2013, the Parliamentary Joint Committee on Corporations and Financial Services presented its report, "Family Businesses in Australia – different and significant: why they shouldn't be overlooked". This report highlighted the importance of the family business sector to the Australian economy, and made a series of recommendations including the establishment of an inter-departmental committee to identify the key policy issues affecting family businesses.

Research strongly suggests that businesses which are able to be passed down from one generation of family ownership to the next are more profitable and more stable: a 2010 Family Business Australia report concluded that family business return on investment is 30% higher than for a non-family business and average debt level is 50% lower than for non-family business; and the average employment period of a family business CEO is 20 years, compared to 4 years for a non-family CEO. More stable and more profitable businesses mean better employment, and more tax revenue. Government should maintain policies which encourage family businesses to stay in family hands, and should enact laws and regulations which make it as easy and painless as possible for generational change to occur, so that family businesses can remain stable and profitable into the future.

However, in many ways the current taxation regime has the opposite effect. Contributors to the Parliamentary Joint Committee report highlighted the following specific issue: the adverse impact of capital gains tax (CGT) on transfers of wealth within family groups. With limited exceptions, transfers of assets between entities or individuals within the same family group are subject to the same CGT consequences as the transfers of those same assets outside of the group. Where assets are transferred between family members at lower than arms-length value (a common arrangement between family members to make generation succession affordable), the Commissioner of Taxation can substitute a higher market-based value for the purposes of calculation CGT on that transaction. The impact of these rules on generational succession is to encourage families to sell assets, including the family business, to non-family third parties which might include overseas companies leading to heightened risk of tax revenue leakage.

Under the current rules, no CGT is payable on transfer of family assets to the beneficiaries of a deceased estate; in that circumstance there is an effective CGT rollover to the new owner of post-1985 assets, while pre-1985 assets are deemed to have been acquired by the new owners at the market value as at the date of death. The message here is therefore: under the current rules, the most tax effective succession outcome is for the existing owners to die.

Submissions to the Parliamentary Joint Committee made a number of suggestions for amendments to the CGT rules, including:

- Re-instatement of the trust cloning provisions previously removed via amendment of Division 104 of the Income Tax Assessment Act 1997; and
- Implementing rollover relief in applicable circumstances, e.g. removing CGT consequences for transfers of assets within defined family groups (including companies, trusts and individuals).

Grant Thornton supports these suggestions.

*38. In what circumstances is it appropriate for certain types of businesses to be subject to special provisions? How can special treatment be balanced with the goal of a fair and simple tax system?*

It is our view that special provisions and exemptions should generally not be available, as such provisions invariably increase the level of complexity in the system.

However, we believe that there are circumstances where the benefits from such targeted support outweighs the simplicity argument.

For example, we note the budget benefits provided to small business and seek that such benefits be extended to the MSB sector.

Furthermore, industries or sectors viewed as important to the Australian national interest, long term economic prosperity, or pivotal in delivery of quasi-public services (not-for-profit) may warrant special treatment.

Overseas experience has shown that concessions in the innovation area have proved to stimulate economic growth and assist in keeping intellectual property from moving offshore. For example, support to technology start-ups and improvements to employee share and option plans have already been identified as areas which would benefit, in supporting the continuation of Australian innovation.

We would also reaffirm our view that consideration be given encourage Australian producers and increase exports, either through greater concessions for local investment (such as the reintroduction of investment allowances) or possibly even concessionary tax rates on export sales to local producers.

# Research and Development

## Discussion questions

*39. Does the R&D tax incentive encourage companies to conduct R&D activities that would otherwise not be conducted in the absence of government support? Would alternative approaches better achieve this objective and, if so, how?*

A more holistic assessment of the impact of the R&D tax incentive needs to be taken rather than focussing on whether or not the R&D would have been undertaken anyway. For start-ups and mid-size business, the refundable tax offset is an important source of cash which allows the R&D to continue. An internet search will quickly reveal announcements listed companies have made to the market in relation to the R&D refunds and how they will be used in their future developments. There are also announcements in the public domain of how refundable R&D tax offsets have encouraged companies to come to Australia to undertake R&D. The policy which sought spill over benefits to the wider community is therefore on the path to achieving this aim – more work and potentially different work for our researcher community. This can only add to Australia's knowledge base.

A search of global R&D tax incentives reveal any number of mechanisms by which governments target supporting R&D. There are many positives of the Australian R&D incentive. Firstly it provides companies with cash. Deductions may have future value, dependent of course on whether the integrity measures are satisfied. Cash has immediate value and use. The Australian R&D incentive is also relatively straight forward in terms of administration and calculation of the amounts – again a positive. By having the mechanism of support through the tax also has the advantage of allowing companies to undertake R&D on the matter/field of their choosing. It means a wide range of projects can be undertaken under the program. This can be contrasted with grants for instance, which would require companies to undertake R&D on subjects which grant providers thinks is of importance.

The R&D tax offset program has been in place for approximately 2 years and all indications are that it has been taken up and worked into company's R&D program, leading into future commercialisation of new offerings.

*40. What other taxation incentives, including changes to existing measures, are appropriate to encourage investment in innovation and entrepreneurship?*

Suggested changes to the existing R&D measures would be to reconsider the introduction of quarterly refunds to allow more immediate cash flow benefits to be realised by claimants. It is also strongly recommended that no further reductions related to expenditure caps or the rate of the tax offset be considered. Changes of these types introduce uncertainty and can impact investment decisions.

Seed and early stage funding is critical to innovation and entrepreneurship. Tax incentives designed to assist smaller higher-risk businesses would encourage seed and angel investors to fund innovation and entrepreneurship.

This could be achieved by offering a range of tax reliefs to investors who purchase new shares in those companies. An example of such a scheme is the UK Enterprise Incentive Scheme which is designed to help smaller higher-risk trading companies to raise finance by offering a range of tax reliefs to investors who purchase new shares in those companies.

# Not-for-profit sector

## Discussion questions

### *47. Are the current tax arrangements for the NFP sector appropriate? Why or why not?*

Broadly we consider the current income tax exemption for the NFP sector is appropriate. Income tax exemption is offered to NFP entities that pursue particular altruistic purposes without having to consider the activities undertaken to pursue that altruistic purpose. The test of whether an entity is pursuing its altruistic purpose is a straightforward one.

We would not generally support a move to greater focus on the activities that an NFP entity undertakes because this would create additional complexity and compliance for NFP entities. Such complexity and compliance provides a barrier to entry for new NFP entities and diverts resources away from NFP entities altruistic purposes.

Increasingly Australian based NFP entities are facing competition from foreign based NFP's who establish operations in Australia. Various requirements of the income tax exemption and deductible gift recipient (DGR) regimes impose requirements that require NFP entities be in Australia or carry on their activities in Australia. This places Australian based NFP entities at a competitive disadvantage because they compete with foreign based NFP entities that have access to global resources. When an Australian based NFP entity looks to expand overseas to build a global footprint and access resources the current income tax exemption and DGR regimes limit their ability to compete.

Entitlement to deductible gift recipient status is complex and difficult for NFP entities to understand because it is not properly aligned with the income tax exemption regime. We would support the broadening and simplification of the entitlement to DGR so that the broader group of income tax exempt NFP entities were automatically entitled to DGR status. This would enhance the fund raising capacity of the sector and reduce reliance on alternative forms of government and other funding. Specific classes of income tax exempt entity could be excluded from the DGR regime. Where NFP entities did not want to comply with the additional compliance requirements associated with DGR they could choose to opt out.

Entitlement to exemptions from various State taxes should be standardised to be in accordance with requirements for Division 50 exemption for income tax purposes.

### *48. To what extent do the tax arrangements for the NFP sector raise particular concerns about competitive advantage compared to the tax arrangements for for-profit organisations?*

Tax arrangements for the NFP sector are appropriate because they support the furtherance of the pursuit of altruistic purposes. The NFP sector is becoming more sophisticated and diverse in response to a range of challenges with the result that increasingly the NFP sector is competing with the for-profit sector.

Any reform of the NFP sector to align its treatment with the for-profit sector will create compliance costs for the NFP sector and inevitably reduce the resources available to meet altruistic purposes. Such an outcome would result in an increased reliance on government funding to fill the gap. As such reform should be targeted at specific concerns so that the majority of NFP entities are not affected.

*49. What, if any, administrative arrangements could be simplified that would result in similar outcomes, but with reduced compliance costs?*

There are a number of areas where the taxation of NFP's can be simplified:

- The tax exemption regime should be harmonised across taxes, including stamp duty, imposed by all levels of Government. Currently entities within the sector are incurring costs dealing with multiple regimes across taxes imposed at each level of Government
- Revamp donation rules so that DGR's can provide limited benefits to donors without impacting the definition of donation. Current guidelines are complex, particularly as they relate to fund-raising functions and events. Simplifying these rules will encourage fund raising activities by DGRs and reduce the need for government support.
- Replacing the NFP FBT concessions with a direct subsidy to NFP employers or employees of NFP entities. The complexity and cost of the administration of benefit arrangements limits the ability of some NFP entities and employees to access the full benefit of the FBT concessions at a reasonable compliance cost. Introducing a direct subsidy would reduce costs and provide a subsidy for employment that was distributed equitably to NFP entities and employees.

*50. What, if any, changes could be made to the current tax arrangements for the NFP sector that would enable the sector to deliver benefits to the Australian community more efficiently or effectively?*

Changes should be made so that an employee of an NFP entity is entitled to only one FBT cap in each FBT year. Currently employees can benefit from multiple caps where they have multiple employers during the year. We consider that a requirement for employees to indicate on their employment declarations that they have been (or are) in receipt of concessional FBT benefits from another employer in the same FBT year is a workable solution that would not impose an unacceptable compliance burden on affected employers.

# GST and state taxes

## Discussion questions

*51. To what extent are the tax settings (that is, the rate, base and administration) for the GST appropriate? What changes, if any, could be made to these settings to make a better tax system to deliver taxes that are lower, simpler, fairer?*

### Background

When first proposed it was intended that GST that would replace all existing sales taxes, as well as applying to all goods and services, similar to the New Zealand GST regime. In 1998/99 the Liberal government initially stated that exemptions to the GST were not possible as this would impact the efficiency of the GST. A prominent selling point of the GST legislation was that all the revenue raised by the GST would be distributed to the states and territories.

GST was introduced in Australia on 1 July 2000 to primarily replace the Australian Government's wholesale sales tax which had become complex and had a multitude of rates. GST also, with the agreement of the states and territories, was to replace a number of narrow-based state and territory taxes. In 2008 the states and territories reaffirmed their commitment to abolish and not reintroduce the state taxes initially identified for abolition. However, some States have, to this day, deferred their obligations to abolish certain of these taxes.

The GST system that was ultimately introduced in Australia was neither like the New Zealand GST system nor was it entirely as envisaged by its initial proposers. Due to the inclusion of a relatively high number of exemptions in the GST law the breadth of application of GST was significantly reduced. This in itself is not unusual in that GST/VAT systems with wide-ranging exemptions similarly exist in most other developed countries. Nonetheless, there seems little doubt that the allowance of these exemptions has reduced the scope and effectiveness of the GST system.

Australia's GST rate, currently at ten per cent, sits at roughly half of the average GST/VAT rate among OECD countries. It is one of the lowest rates in developed countries worldwide although the rate is higher than that of regional neighbours Singapore and Malaysia and the same as the rate in Indonesia.

In 2012, the average OECD GST coverage rate was 55 per cent whereas the Australian GST coverage rate was only 47 per cent (and the New Zealand GST coverage rate was 96 per cent). This percentage also represented a fall in the coverage rate of 9 per cent from its peak in 2005/6. Since 2002/3 GST revenue has consistently declined relative to the size of the Australian economy. It is considered that this is due to a decline in household consumption as a percentage of GDP as well as a shift to consumers spending on those items exempted from GST.

Therefore, in light of the above the GST system in Australia must be considered, in relative terms, to be delivering less revenue overall to the Australian government than most other developed countries due both to its low rate as well as its below-average coverage caused by the relatively high number of exemptions. Further, it is also arguable that the GST system has not kept track with consumer spending patterns and has become at least to some degree out-dated. It is, however, fair to note that Australia's GST system is not alone in this regard as GST/VAT systems primarily designed in the 1970's struggle to cope with the intangible cross-border and e-commerce transactions of today's world.

### Reform options

As noted above a decline in household consumption as a percentage of GDP as well as a shift to consumers spending on items exempted from GST has seen GST revenue decline relative to the size of the economy since GST was introduced on 1 July 2000. The Australian GST system is, therefore, in need of urgent reform to deliver on its early promises.

A GST system still represents one of the most economically efficient ways to boost government tax collections through a stable and growing source of revenue. However, by comparison on a global basis to OECD and developed countries, the Australian GST system has a very low rate of GST as well as low coverage. This, together with its inherent complexity caused by a range of complicated exemptions, leads to an obvious conclusion that the current GST settings (rate, base and administration) are not appropriate.

We consider that reform to the system is required for the GST system to not only deliver as was initially envisaged at the time of its introduction but also to operate effectively in a modern economy as part of a broader range of tax measures. By comparison with developed nations and other OECD countries VAT/GST systems the rate and coverage of GST as well as its inherent complexity could be considered to be inappropriate.

To have a more effective and efficient GST system the government has a range of options available to it:

#### Increase the rate of GST

An increase in the rate of GST would provide additional GST revenue which would flow through the economy and provide more funding for the states and territories, assist in paying for infrastructure and assist in alleviating the budget deficit. Increasing only the GST rate also means that the existing GST administration system would not need significant change.

An increase in the rate of GST would represent a change for businesses, having an impact on their systems, processes, pricing structures and relationships with suppliers, clients and customers. This would require work for all GST-registered businesses as business systems would have to be changed. However, a simple change of rate with no shift in the base to which GST applies would minimise disruption to business.

There may be an impact on low income earners but to alleviate this government could provide a level of support through mechanisms such as reductions in personal income tax and social subsidies.

#### Broaden the base of supplies to which GST is applied

As noted above exemptions distract from the simplicity and increase the complexity of the GST system. Therefore, a move closer to the basic principles on which Australian GST was founded, with the tax being applied more broadly to goods and services could be considered.

Government could, therefore, consider the reasons exemptions were initially given and whether these reasons are still relevant today with a view to determining whether it is still appropriate to provide GST-free treatment (i.e. to education, child care, healthcare, supplies of precious metals, sales of certain farmland etc.).

A broadening of the base would represent a significant change for some businesses, having a major impact on their systems, processes, pricing structures and relationships with suppliers, clients and customers. This would require not insignificant work to be done by affected businesses as significant changes to business systems would be required. This change would likely be more significant from a business system perspective than any change resulting from a simple rate increase.

A removal of some of the exemptions currently enjoyed, given where the exemptions are depending on which exemptions are removed (i.e. health, education, child care), could have a more significant impact on low-income earners than a rate increase. As noted above the government could consider introducing more targeted social services and support mechanisms to compensate.

#### Move certain supplies from within the GST-free schedules in the GST act to the Input Taxed schedules

Input taxed goods and services have some GST embedded in their prices but not the full ten per cent. This is because suppliers cannot claim an input tax credits on costs related to making input taxed supplies. Therefore, in simple terms input taxed goods and services are not fully taxed but “partially taxed”.

The government could consider making changes to the GST legislation which would remove the GST-free treatment enjoyed by certain goods and services and instead treat these goods and services as input taxed. This would increase the collections of GST revenue by the government but lessen the blow that would be felt by removing GST-free treatment entirely. Such changes could be more palatable to low income earners and businesses alike.

However, this measure alone would be likely to have a modest impact only on GST revenue collected. Further, changing GST-free supplies to input taxed would be extremely complex, time-consuming and costly for businesses which would be required to make significant and complex changes to business systems, processes, pricing structures and it would impact their existing relationships with suppliers clients and customers.

#### Summary of Grant Thornton Australia position

Based on the above we propose that the government introduces one or all (to some degree at least) of the following to create a more effective and efficient GST system:

- 1 A GST rate increase;
- 2 A broadening of the base of supplies to which GST is applied;
- 3 Movement of certain supplies from within the GST-free schedules in the GST Act into the Input Taxed schedules

We propose these changes are not made in isolation but in the wider context of the removal of inefficient and ineffective taxes, such as stamp duties, at State level.

At the very least we propose an appropriate increase in the rate of GST. To the extent that a higher rate increase (such as 15%) is not determined to be palatable from a social perspective and instead a lower increase (such as 12.5%) is instead introduced it is our belief that this would not alone deliver Australia with the required GST revenue nor would it be on par in relative terms with that obtained by most other developed nations and its OECD counterparts. If the only change to the GST system involved a modest change to the GST rate it is our view that the Australian GST system would continue to lag behind other GST/VAT regimes both in terms of its GST rate and breadth of coverage.

If a lower rate of increase is introduced we would recommend that serious consideration is given to introducing this rate increase together with other GST amendment measures such the broadening of the base of supplies to which GST applies and/or the shifting to input taxed treatment some supplies which currently enjoy GST-free treatment. In considering which exemptions should be retained or removed the government should consider fully the reasons why some of the current exemptions were offered initially and determine if these reasons are still relevant and supportable today and in relation to the Australian current economic position.

An increase in GST rate and/or a broadening of the base will represent a significant change for businesses, having an impact on their systems, processes, pricing structures and relationships with suppliers, clients and customers. It may also come as a shock to the Australian public, in particular low-income earners and so the process of change would need to be carefully managed with changes made in the context of a wider package of reform measures aimed at compensating those badly affected. Nonetheless, it is important that the Australian public is asked to recognise how far below most other OECD countries the Australian GST currently is in terms of rate, size of the base and revenue collected. It also needs to be pointed out that the revenue collected from GST has been constantly declining since 2004/5 relative to the size of the Australian economy.

We also acknowledge that the 2008 Intergovernmental Agreement on Federal Financial Relations and the A New Tax System (managing the GST Rate and Base) Act 1999 require any changes to the GST rate or base to receive unanimous support of the state and territory governments and the passage of the relevant legislation by both Houses of the Australian Parliament. Nonetheless, it is our view that the fact that this may be difficult to achieve and that changes to the GST system may be unpopular with the electorate is simply not a good enough reason to not push ahead with making necessary changes to a GST system which is not delivering what it should for the Australian economy.

Overall, we note that any GST reform should not be considered in isolation, but should instead form part of a wider review of our entire tax system, incorporating improvements in administration, reduction in unnecessary red tape and incentives and further concessions to encourage Australian businesses as well as to encourage overseas investment in Australia. For example, similar to at the time of introduction of GST the Government could consider reform to individual income tax and family payments to partially compensate for a net increase in GST at the same time agreeing with state and territory governments to abolish or significantly reduce inefficient and ineffective local taxes.

*52: What are the relative priorities for state and local tax reform and why? In considering reform opportunities for particular state taxes, what are the broader considerations that need to be taken into account to balance equity, efficiency and transitional issues?*

There are currently too many State taxes. Many of these vary significantly across the States, which also creates further confusion. Grant Thornton is of the view that State taxes should be streamlined further and removed (where possible).

The extent to which the above can be achieved will depend on the ability to achieve other tax reform, such that additional revenue can be provided to the States to offset against the revenue that they will lose. The broadening of the GST base and the increase in the GST rate are examples of reform that would increase the revenue that could be distributed to the States.

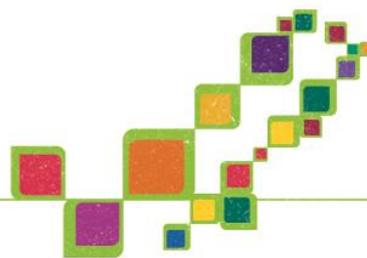
Priorities for consideration include:

- **Payroll tax** - The tax white paper refers to payroll tax as an efficient way to collect tax. However, payroll tax can potentially be a disincentive for businesses that face high wages, increasing compulsory employer superannuation contribution obligations, as well as other obligations (such as worker compensation insurance) when employing workers. Increasing the payroll tax rate or decreasing the payroll tax exemption threshold would only make Australia even less competitive in the global market. Further, payroll tax continues to create substantial administrative work for businesses that operate across more than one State, even after legislative changes in recent years.

- **Stamp duties** - The tax white paper refers to municipal rates as being an efficient way to raise tax. It also states that land tax exemptions for principal place of residence and primary production land reduce the potential land tax base by more than half. Further, stamp duty is seen to be an extremely inefficient tax that discourages movement and increases house prices.

The removal of stamp duties could potentially be more palatable to the States if:

- the land tax tax-free threshold were removed or decreased; and/or
- the land tax rates were increased; and/or
- the available land tax exemptions were removed or reduced; and/or
- the municipal rates calculation were altered; and/or
- transitional provisions were enacted to grandfather previous transactions



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