JUNE 2015

RESPONSE TO TAX DISCUSSION PAPER

RETAIL COUNCIL

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Table of Contents

List of Tables

Abbreviations

Gross Domestic Product	GDP
Goods and Services Tax	GST
Low Value Threshold	LVT

ABOUT THE RETAIL COUNCIL

The Retail Council is the voice of Australia's top retailers driven to achieve sustainable growth of retail in Australia for the benefit of the consumer, the industry and the economy.

Formed in 2006, the Retail Council represents members committed to advancing retail in Australia, fostering economic growth and supporting job creation. They are retail businesses that lead the industry delivering to customers across all types of retail goods and services and are leading employers who contribute to local communities and regional development and strongly interrelate with other Australian industries.

As an authoritative voice of Australia's top retailers, the Retail Council contributes to the development and support of public policy that would boost productivity, support employment growth, foster a competitive environment and ultimately make the sector stronger.

Retail Council members are part of an industry that is a top ten contributor to Australia's Gross Domestic Product (GDP) contributing more than $134 billion (or 8%) of total economic activity through more than 127,000 retail operators nationwide and providing jobs to more than 1.25 million Australians.

EXECUTIVE SUMMARY

The Retail Council welcomes the opportunity to contribute to the Tax Reform White Paper process, including providing feedback on the initial stages of this process in the form of the *Re:think* Discussion Paper.

This review of the tax system is timely given the significant structural change that has taken place in both businesses and households since much of the system was designed and given the challenges that lie ahead.

Australia needs a tax system that reflects a modern Australian economy that operates 24/7 and competes across almost all aspects on the global stage for capital, labour and customers.

Australia needs a tax system that reflects a modern Australian that is ageing, seeking broader flexibility in work arrangements while also facing cost of living pressures and affordable housing challenges.

In short, the tax system is no longer fit for purpose and change is needed.

Tax reform matters to retailers on two levels.

Firstly, via the direct impact the tax system has on retail businesses through a range of areas such as company taxes, indirect taxes and GST.

Secondly, retailers also focus on the tax system because of the impact it has on the two most important components of our businesses – customers and employees. This means areas such as personal tax, retirement and savings taxes and fringe benefits tax are important for retailers.

At this early stage in the White Paper process, the Retail Council has focused on a principle based approach which looks at the key pillars the tax system should be built on.

- The tax system should be fair
- The tax system should drive growth
- The tax system should be simple and efficient
- The tax system should provide an adequate safety net

The White Paper process needs to keep these principals top of mind when examining how to redesign Australia's tax system so that it is both fit for purpose and able to raise sufficient funds to sustain Australians both now and into the future.

It is important that any proposed changes are considered in the context of the whole system. Tax increases or base broadening in one area should be offset by tax reductions - or removal – in other areas. For example, any increase in the GST or broadening of the base must be accompanied by the removal or reduction of taxes in other areas such as personal income tax and state taxes.

The following table summarises the examples within this submission that the Retail Council encourages the Government to consider when formulating the Green and White papers in the coming months.

Table 1: Summary of specific areas for consideration

Issue	Details	Page
Interaction of welfare and income tax system	A well-functioning tax system needs to ensure that it interacts with the welfare safety net appropriately so that employees do not face high marginal tax rates as they increase the hours they work.	13
Bracket creep	Bracket creep needs to be avoided as it reduces the progressivity of the tax system and, for some employees, may result in reduced participation.	14
Complexity of personal income tax system	The personal income tax system needs to be simplified, including the FBT system.	14
All companies should face the same company tax rate	The cut in the company tax rate for businesses with turnover of less than $2 million should be extended to all businesses – as initially proposed – to ensure that the tax system does not distort the competitive process.	16
Australia's company tax rate needs to better balance competitiveness and sustainability	Australia's company tax rate of 30% (or 28.5% for companies with turnover under $2 million) needs to be more internationally competitive.	16
GST	Any consideration of changes to the GST base and rate must be considered against the personal income tax system to ensure that the overall individual tax system maintains its progressivity. The GST tax system needs to be sustainable within a broader tax system, especially as it funds important state-level services such as hospitals, education and policing.	19
Similar transactions are subjected to the same GST treatment	The LVT for GST on imported consumer goods should be reduced to zero so that all goods and services are treated the same under the GST system, no matter how they are purchased.	19
Administrative complexity of the GST	A more timely and cost effective approach is needed to GST administration.	21
Harmonisation of state taxes	Businesses with multi-state operations must navigate not only different tax rates by states for payroll tax, stamp duties and land tax – but also different tax base definitions. COAG progress regarding state tax harmonisation has been too slow.	21
Consolidation of state taxes	There is an opportunity in the review of the tax system to reduce complexity in the system by removing the number of taxes, in particular state taxes.	21
Hypothecating fuel excise for road maintenance and upgrades	Fuel excise revenue should be completely directed towards improving roads.	23
Complexity of alcohol taxes	The alcohol excise system needs to be simplified.	23

OVERVIEW OF THE RETAIL SECTOR

This section outlines the importance of retail to growth, jobs, the broad economy and the tax system.

Retail contribution to growth and jobs

The retail sector directly accounted for more than $71 billion of economic activity or 4.5 per cent of the national economy in 2014. This represents a share of total industry value-added twice that of agriculture, forestry and fishing. In addition, retail supported another $63 billion of activity, or 4 per cent of GDP, in connected industries.

The most positive contribution retail makes to Australia, however, is not necessarily measured in terms of dollars – it is how many jobs retail creates and supports. Retail is currently responsible for directly employing 1.25 million Australians; providing career opportunities for customer service professionals, butchers, bakers, pharmacists, hairdressers, mechanics, financial analysts, information technology and communications specialists, human resources managers and more.

Indeed, the retail sector is Australia's largest private sector employer, accounting for 11 per cent of Australia's workforce.[1] In addition, retail supports approximately 500,000 jobs in other sectors across the economy, including food manufacturing, agriculture, transport and construction.[2]

Around half of retail jobs (605,000) are part-time roles which allow flexibility for a modern workforce particularly primary care givers and young people wanting to combine family and/or study commitments with employment.[3] Retail is also the second largest employer of women – over 690,000 women work in the sector, with around 420,000 working part-time.[4]

Retail has one of the youngest age profiles of any workforce, with around one third of retail staff aged 24 years or younger.[5]

Retail is also a major employer of mature aged workers, employed around 168,000 people aged over 55.[6] The number of mature aged retail employees has increased by 50 per cent over the past decade.

The flexibility and diversity of the retail workforce allows the sector to meet the demands of the modern consumer, to be able to shop how they want, where they want and when they want.

The Retail Council's members' commitment to their customers extends to the diversity of the workforce, ensuring that the retail team reflects the customer. Our members have a range of initiatives to increase diversity in the workplace, particularly mature age workers, indigenous people and people with a disability.

[1] ABS (2014), 6291.0.55.003 Table 5 – Employed persons by State and Industry.

[2] ANRA (2011) Retail is jobs

[3] 6291.0.55.003 - Labour Force, Australia, Detailed, Quarterly

[4] 6291.0.55.003 - Labour Force, Australia, Detailed, Quarterly

[5] 6291.0.55.003 - Labour Force, Australia, Detailed, Quarterly

[6] 6291.0.55.003 - Labour Force, Australia, Detailed, Quarterly

Retail is over 125,000 businesses

The Retail Council represents Australia's top retailers including listed companies, private companies, and franchises supporting many thousands of small businesses. Approximately one third[7] of all sales annually are transacted in 122,000 small businesses, with the remainder occurring across over 5,000 medium to large enterprises. These 127,000 retail operators represent about six per cent of all businesses across Australia.[8]

Structural change in retail

Retail has been, and always will be, about delivering a broad range of products that customers want at affordable prices. Retailers guide customers through the entire purchase process, from researching products through buying and finally to using their purchases. In the past decade, however, the way in which customers engage with retailers to execute this purchase process has changed dramatically. The internet has 'disrupted' the sector but more importantly it is providing new opportunities for retailers that embrace this change.

The initial impact of online retailing was the emergence of new online-only stores, many of which were located outside Australia.

In the next stage of this change, existing bricks-and-mortar stores established online divisions of their businesses to give customers the type of service models they were seeking.

Most recently, a new type of retailer has emerged that is both online and store-based and delivers this service to customers seamlessly – the omni-retailer. These retailers have operating systems that are completely connected, rather than operating the online business separately under different logistics systems. Customers have the same purchasing experience, no matter how they choose to interact. Omni-retailers operate and structure their business completely around the customer.

These structural shifts mean competition in the retail market is changing as Australian retailers compete beyond borders.

The implications of this structural change, in terms of the tax system, are that it is no longer fit for purpose. The current tax system was designed at a time when retail was an in-store and domestic-based sector. Competitors were stores located in the same street not those located anywhere in the world.

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[7] ABS (2015), 8501.0 Table 14 – Retail Turnover, Completely Enumerated (Large) and Sample (Small), By Industry Group.

[8] as at June 30, 2013 in ABS (2014), 81650 – Counts of Australian Businesses.

IMPORTANCE OF TAX REFORM FOR RETAIL

The Retail Council believes the current tax system needs to be better designed so that it reflects the modern economy, rather than the economy of many decades ago, when some of the tax laws were written, with lots of ad hoc add-ons.

The tax system must be appropriate for the modern Australian economy.

Major tax reform is not an easy undertaking, but it is not an impossible task – this was demonstrated by the successful introduction of the GST in 2000. The key is to develop well-articulated arguments that explain to taxpayers why the change is being proposed and what the actual impacts will be in both the short and long term. Australian history shows that Government's that make their case can instigate change.

Current contribution of retail to the tax system

The retail sector makes a significant contribution to the tax system via both payments directly paid by the sector and the tax collected by the sector on behalf of the Government, in particular GST.
Retailers disburse approximately $3.4 billion in company tax per year – more than 5% of all company tax payments across all industries.

Retail employees earned almost $40 billion in pre-tax wages in 2012/13, much of which is then spent in the Australian economy, supporting other sectors and jobs.[9]

Estimates published in the Henry Tax Review[10] showed the retail sector has one of the highest effective company tax rates of any industry in Australia. At 27 per cent, this was equal highest (with the finance sector) and well above the industry average (24%) and other sectors such as mining (17%), IT (14%), transportation (22%) and construction (23%).

The Henry Tax Review attributed some of these biases to differences in capital allowance arrangements for capital works (according to asset type) and the deductibility of exploration expenses; and also the taxation of industries more generally (notably agriculture and forestry). One thing that is clear is that some industries certainly benefit from inconsistencies in Australia's approach to company tax.

Research performed by the University of Technology, Sydney, also suggested that medium-large retailers paid one of the highest effective corporate tax rates (29%) of all industries in 2011/12 –well ahead of the average for all industries of 26 per cent.[11]

The total tax rate for retailers – after all Federal, State and Local taxes are taken into account – is estimated to be in the order of 45 per cent; which is again one of the highest across all industries.[12]

[9] 8155.0 Australian Industry, 2012/13

[10] Australia's Future Tax System (2010) (chapter 5: Investment and entity taxation, of Part 1: overview), p.40

[11] Lanis, R. (2014) Who Pays for Our Common Wealth? Tax Practices of the ASX 200

[12] PwC (2011), Total 2010 Total Tax Contribution: Understanding the economic contribution of business.

Current tax system impacts on retail growth and productivity

The Retail Council believes the current tax system does not match shifting economic structures and that 'tinkering' with the tax rules will not be sufficient to provide the type of tax system Australia needs in the future. Australia's tax system has not kept up with the structural change and internationalisation of the Australian economy, including retail, in the past decade. Retail is now a cross-border industry that competes for customers, staff and capital in a global marketplace. As such, the tax system is inhibiting the growth potential of Australia.

A redesigned tax system should broadly meet four key principles – none of which is adequately addressed in the current tax system.

1. Tax system should be fair

Fairness or equity is an important aspect of the Australian system. Much of the focus in the *Re:think* discussion paper is rightly around fairness and relates to the personal income tax system, in particular the interaction of the tax system and welfare system. But fairness is also important –and currently lacking - in the business tax system. Different retailers face different company tax, GST and depreciation regimes.

For example, consumer purchases of goods and services sold by overseas-based companies worth less than $1000 are not subjected to GST. This makes the playing field uneven.

Depending on company structures, some international competitors are not subjected to the same company tax liabilities as Australian retailers. Within Australia, small retail competitors now operate under a different tax regime, with a lower company tax rate and different depreciation rules.

A key priority for retailers in any redesign of the tax system is to improve its fairness, across all taxes including the business and personal systems.

2. Tax system should drive growth

The tax system needs to be redesigned to ensure that it is not discouraging businesses to invest or employees to increase workforce participation. The tax system should encourage, not discourage growth. This will be increasingly important as the population ages and as the economy becomes more internationalised.

There are two key inputs into any business – labour and capital. The current tax system is inhibiting access to these two important inputs and thus impeding economic growth.

For example, high effective marginal tax rates, especially for second-income earners or part-time employees, discourage some employees from increasing their working hours. This is particularly a problem for a sector such as retail which has almost half of its employees working part-time.

Similarly, the tax system is also impeding access to capital. As an internationally competitive sector, Australian retailers need to be able to attract capital for investment and expansion. Local retailers are competing on international capital markets for such funds, not just against locally-based competitors. Retailers with international parents are competing for investment for store renewal against other geographies that provide better return on that investment. It is difficult for Australian retailers to raise funds from capital markets abroad. This is because the return on investment for a non-resident buying into an Australian retail company is dramatically less than a retail company in other developing countries, due to Australia's higher than average corporate tax rate, and the inability for non-residents to claim credits for underlying taxed paid in Australia due to the operation of Australia's imputation system. Australia's corporate income tax rate, and overall collection of inefficient income taxes from all businesses, irrespective of structure, needs to be significantly reduced to enable Australia to compete on the world stage. The size of the reduction should be set with reference to prevailing and anticipated future corporate tax rates of countries around the world.

Part of the focus on growth and productivity gains should also involve looking at the efficiency of taxes, and changing the balance of the tax system away from taxes that are most distorting on behaviour and economic activity.

3. Tax system should be simple and efficient

Reducing complexity should be a priority. The impacts of the tax system are broader than the actual amount of tax paid; the manner in which tax is collected and the cost of collection also impede performance of the sector.

Compliance costs are particularly high for retailers that operate across state boundaries. States not only have different rates of state-based taxes, such as payroll tax and stamp duties, but also have different calculation rules. This lack of harmonisation of state-based tax systems means each company is required to operate multiple state based tax departments which reduces the potential benefits of scale that large organisations would otherwise be able to pass on to customers.

The GST classification system is complex, especially around the treatment of food. The GST classification of food defaults to GST free under the current law, unless the food item is listed in Schedule 1 of the GST Act as a 'food that is not GST free'. There are only 32 items listed here but there is additional complexity because the schedule applies to food 'similar to those 32 items that are listed'. Conversely Schedule 2 of the GST Act covers beverages that are GST free, under the GST law, beverages default to taxable unless one of the exemptions under Schedule 2.

Some specific examples to highlight the complexity and inefficiency include:

- Plain Milk is GST free whilst Flavoured Milk is taxable.
- Natural Water without additives is GST free whilst Sparkling Water is taxable.
- Fruit Juices with 90% or more natural juice content are GST free whilst becoming taxable below this percentage.
- A Sara Lee Frozen Cheesecake is taxable as a Cake whilst a Sara Lee Chocolate Bavarian that is also frozen and sits next to the Cheesecake is GST free as a cold set dairy dessert.
- Yoghurt can be taxed a number of different ways depending how it is sold to the customer, for example a yoghurt tub is a GST free dairy offering, a frozen yoghurt is taxable as an ice cream food and a yoghurt smoothie sold in the dairy area is a taxable beverage.

This small example of basic items and the differences in classification of the products shows the complexity that currently exists.

The personal tax system is also so complex that many individuals that should have straightforward tax affairs still feel they need assistance from tax advisers. In addition, many taxpayers pay an amount of tax that they end up getting back through the welfare system. Consideration should be given to ways that reduce this 'churn' of the tax and transfer systems.

These compliance and red tape matters mean businesses divert resources towards navigating a complex tax system rather than focus on their key business of serving customers.

4. Tax system should provide an adequate safety net

One area that the *Re:think* discussion paper did not discuss, which the Retail Council considers important, is the issue of how much revenue needs to be raised. A sustainable tax system, by definition, is one that raises sufficient revenue to fund the future government-provided services that the population seeks and expects. As a result, the tax review process also needs to look at the likely amount of tax that will need to be raised into the future in order to deliver the services and safety net that the Australian community desires.

Some nations opt for a low social safety net and a low tax regime, such as Singapore, Hong Kong and the US. In contrast, other countries seek a large social safety net that needs to be funded by a significant level of tax, such as the Scandinavian model. Traditionally, Australia has fallen somewhere between these models. The public reaction to the 2014/15 Budget suggests that there is not currently a public appetite to move towards a US style model.

The Intergenerational Report[13] highlighted some of the challenges facing Australia as an aging population reduces the number of tax payers. However, a clearer debate and decision around the services Australians want to have funded by governments into the future is needed if the tax system is to be sustainable. This discussion needs to be taking place in tandem with this tax review process so that Australian's can better understand the purpose and aim of tax reform.

The Intergenerational Report indicated the current Australian Government is seeking to have spending that is worth 25.9 per cent of GDP by 2054-55.[14] This compares to the current spending to GDP ratio of 26.2 per cent.[15] However, the Intergenerational Report did not provide details about the type of services and safety net this would deliver to Australians in 2054-55 and how different it would be from the current service levels and priority areas.

This 'target' spending level of 25.9 per cent of GDP is also above the current revenue to GDP level, which is at 23.9% of GDP. This suggests that the overall proportion of tax raised needs to increase and indeed the forward estimates forecast this. This does not necessary mean higher tax rates; it could also be achieved via faster economic growth that generates more tax revenue. Importantly, the Intergenerational report highlights that this will need to be done against the background of a reduced proportion of the population paying personal income tax.

As part of the White Paper process, the Retail Council would welcome a broader discussion of about how much tax needs to be raised to meet the services and safety net Australians want into the future.

Remainder of submission

The remainder of the Retail Council's submission takes these four principles and applies them to the areas of the tax system identified by the *Re:think* discussion paper.

[13] Commonwealth of Australia (2015) 2015 Intergenerational Report Australia in 2055

[14] Commonwealth of Australia (2015) 2015 Intergenerational Report Australia in 2055 p 49

[15] Commonwealth of Australia (2015), 2015/16 Budget Paper No 1, p 3-14

At this early stage in the White Paper process, the Retail Council has focused on a high level principle response for many areas. After more concrete options have been put forward by the Government, the Retail Council will provide feedback on these specific proposals in its response to the Green Paper.

PERSONAL TAX ISSUES

Why is the Retail Council interested in this issue?

The retail sector does not directly pay personal income taxes, however, this aspect of the tax system impacts on two important groups for retailers – employees and customers. As a result, the Retail Council has an interest in ensuring this aspect of the tax system is well designed.

The tax review presents an opportunity to improve around all four of the previously identified desirable tax principles – fair, supports growth, simple and sustainable – within the personal income tax system.

The personal income tax system needs to be fair by ensuring that progressivity is maintained and that all types in wage derived income are treated the same.

The personal income tax system needs to be growth supporting by ensuring that it does not impede labour force participation and appropriately interacts with the welfare system.

The personal income tax system needs to be simple so that compliance costs are kept to a minimum for individuals and companies. Under Australia's self-assessment system, most tax payers should be able to complete their tax returns themselves (or not need to lodge one) and understand their tax obligations. There also needs to be greater harmonisation in terms of income definitions that are used to assess eligibility for welfare payments.

The personal income tax system needs to support a sustainable overall tax system, especially in the context of a falling proportion of the population paying personal income tax as the population ages.
The Retail Council has identified examples where the personal income tax system currently fails the fair, growth supporting, simple or sustainable tests.

Example 1: Interaction of welfare and income tax system

One of the challenges in designing a well-functioning tax system is to ensure that it interacts with the welfare safety net appropriately so that employees do not face high marginal tax rates as they increase the hours they work. Around half of retail employees are part-time employees, a group that is particularly vulnerable to coming up against high marginal tax rate problems.

For example, a parent may be working part-time as the second income earner in a two-income family that also receives family benefit payments and child care fee relief assistance. As this parent increases the hours they work, they will also have a reduction in the amount of family benefit and child care assistance they receive. In some instances the taper rate of the welfare receipts are such that the effective marginal income tax paid on each extra dollar earned is significantly greater than the marginal tax rate. In some instances, while the marginal income tax may be only 19% or 32.5%, the effective marginal tax rate faced by the income earner will be potentially much higher due to the simultaneous loss of welfare receipts.

This situation clearly has an impact on household finances, but it also impacts on employment growth as it deters some second-income earners from increasing the hours they work. Around half of retail employees are part-time employees, a group that is particularly vulnerable to coming up against high marginal tax rate problems.

Example 2: Bracket creep issues

Participation and equity issues can also be impacted by bracket creep; as the rise in incomes pushes increasing numbers of taxpayers into higher income brackets. This reduces the progressivity of the tax system and, for some employees, may result in reduced participation.

In short, retail customers will be left with less disposable income to spend in the sector and employees will be more likely to avoid increasing their hours.

Personal tax brackets have not been substantially changed since June 2008 and the 2015/16 Budget indicated no plans to do this in the forward estimates. As a result, bracket creep will become an increasing problem into the future in terms of reduced fairness and inhibiting workforce participation in the personal income tax system.

Example 3: Complexity of personal income tax system

There is an opportunity for this review to reduce the complexity of the personal income tax system. Developments such as pre-filling and e-tax have made completing personal income tax returns easier, but there are still opportunities for greater simplification.

The challenge for policy-makers is to better deal with the balance between complexity and integrity. Currently, there are areas of the tax system based on the premise of 'chasing every last dollar' rather than looking at the cost implications of extreme complexity.

A good example of this imbalance is the FBT system. This tax only raises 1.2% of all Federal Government revenue, yet it is extremely costly for companies to administer due to multitude of valuation rules and concessions. It is also a tax that is paid by one group but targeting another i.e. paid by employers but in some instances it bourn by the employees. The review should examine the viability of re-working the FBT system to move the system closer to the arrangements used elsewhere where employees, not employers, are responsible for paying FBT via the usual personal income tax system. Incorporating the FBT system into the personal income tax system, and reducing the complexity of the valuation rules and concessions, would completely remove a tax and greatly reduce the associated costly administration.

SAVINGS TAX ISSUES

Why is the Retail Council interested in this issue?

As with personal income tax, companies in the retail sector do not directly pay tax on savings. Nevertheless, this aspect of the tax system also impacts on member's employees and customers.

The savings tax system also indirectly impacts on retailers via its links to funding infrastructure. Retailers depend on a well-functioning freight and logistics system. This could be funded to a greater extent by Australia's pool of superannuation savings, if tax settings were improved to encourage this.

As a result, the Retail Council has an interest in ensuring this aspect of the tax system delivers fairness, supports growth, is simple and sustainable.

The savings tax system needs to be fair by ensuring that similar savings vehicles have similar tax regimes. The exception to this would be superannuation due to both its long-term nature and that it is compulsory.

The savings tax system needs to support growth by ensuring that it does not inhibit the pool of savings being directed at areas that best add to Australia's growth potential such as infrastructure and Australian company securities. The savings tax system should not distort investment decisions such as encouraging people to invest in loss-making ventures for tax purposes only.

The savings tax system needs to be simple to understand so that Australian's easily can make savings decisions based on returns and timeframes, rather than for complex tax purposes.

The savings tax system needs to work with other important aspects of the system - personal, company and GST – to ensure the overall tax system is sustainable into the future.

The Retail Council acknowledges the work of the Treasury Department in the *Re:Think* discussion paper, which appropriately highlighted the current differences in tax rates on various savings streams, which need to be addressed by this tax reform process.

BUSINESS TAX ISSUES

Why is the Retail Council interested in this issue?

As a major contributor to Australia's system, the retail sector is keen to have a company tax regime that is fair, supports growth, simple and sustainable.

The business tax system needs to be fair by ensuring all companies with Australian operations are subjected to the same tax rate and pay the appropriate level of tax for their level of activity in Australia.

The business tax system needs to be more internationally competitive so it can support growth by encouraging companies to locate in Australia so they can employ Australians and reinvest profits in Australia.

The business tax system needs to be simplified and made fit-for-purpose by this review, so that continual add-ons and complexities are not needed into the future.

The business tax system needs to continue to make a contribution to the sustainability of the overall tax system so that corporate Australia is seen as making a contribution to the overall revenue base of the nation.

The Retail Council has identified examples where the business tax system currently fails the fair, growth supporting, simple or sustainable tests.

Example 1: All companies should face the same company tax rate

The Retail Council welcomes the cut in the company tax rate for businesses with turnover of less than $2 million but believes it should be extended to all businesses – as initially proposed – to ensure that the tax system does not distort the competitive process.

Example 2: Australia's company tax rate needs to better balance competitiveness and sustainability

Australia's company tax rate of 30% (or 28.5% for companies with turnover under $2 million) is comparatively high, especially for the Asia-Pacific region. For example, Singapore's rate is 17% and Hong Kong's is 16.5%.

The competitiveness of Australia's company tax system is becoming more important as the economy, and the retail sector, becomes increasingly globalised. Companies are becoming progressively international entities that operate across global tax regimes. This has resulted in complex company structures that see companies paying most tax in those countries that have the lowest company tax rates, such as Ireland and Singapore.

The Australian Government has recognised this problem and in the 2015/16 Budget indicated it intends to investigate 30 large multinational companies that may have diverted profits away from Australia with the purpose of avoiding tax here.[16] From January 1 2016 any firms found to have not appropriately accounted

[16] Commonwealth of Australia (2015), 2015/16 Budget Speech, p 11

for tax raised from activities in Australia will be fined up to 100% of the penalty (as well as paying the owed tax). Budget papers did not indicate how much the Government expects to recoup from this initiative.

While a welcome step, this is a potentially costly and short-term solution. Longer-term, Australia needs to address the differential between its company tax rates and those of overseas competitor countries by investigating ways to lower Australia's company tax rate for all companies.

Despite its desire for a lower company tax rate in Australia, the Retail Council recognises that any reduction in company tax collections would need to still maintain revenue – either via the company tax take or by increasing the tax take from other parts of the tax system. This is not an easy balance. Nevertheless, given the huge amount of leakage currently underway, some action on the company tax rate is needed.

SMALL BUSINESS TAX ISSUES

Why is the Retail Council interested in this issue?

Members of the Retail Council are themselves medium/large businesses, but many support the small business sector through franchise operations, or as customers of small business. The retail sector as a whole includes many small businesses. Businesses that have a turnover under $2 million can access a range of concessions that are designed to either reduce compliance costs for small operators or encourage greater investment and expansion by them.

The small business tax system needs to be fair, without giving small businesses and unfair competitive advantage. The system needs to recognise that small businesses do not have access to the same level of cash flow or expert tax advice as large businesses.

The small business tax system needs to encourage small businesses to grow into larger businesses and does not create undesirable incentives for small businesses to stay small.

The small business tax system needs to be simplified. One of the main tax concerns of small businesses is the complexity of the system, which diverts business owners away from selling to customers.

The small business tax system needs to sustainable, so that this sector of the economy is contributing to the broader revenue base without the tax burden deterring people from starting and expanding businesses.

GST AND STATE AND TERRITORY TAX ISSUES

Why is the Retail Council interested in this issue?

The retail sector plays an important role in the GST system, as the main collector of the tax for Government. Retailers also have to navigate the complex administration of the GST, such as making decisions about when a pizza roll is a pizza roll.

The GST tax system needs to be fair so that similar transactions are subjected to the same GST liability. It also needs to work in tandem with the personal income tax system to ensure that the overall individual tax system maintains its progressivity. The GST tax system also needs to have integrity and apply the same tax treatment to the purchase of a good no matter how that transaction is carried out and where the retailer is located.

The GST tax system needs to ensure that it is supporting growth rather than acting as a distortion on the competitive process and economic growth.

The GST tax system needs to be easy to implement for retailers and easy to collect and remit. This applies to new businesses that need to be caught in the system such as international retailers.
The GST tax system needs to sustainable within a broader tax system, especially as it funds important state-level services such as hospitals, education and policing.

The Retail Council has identified examples where the GST tax system currently fails the fair, growth supporting, simple or sustainable tests.

Example 1: Similar transactions are subjected to the same GST treatment

When a consumer purchases a good or service it should not matter how that purchase is executed – online or in-store – they should be subjected to the same level of GST. The current $1000 Low Value Threshold (LVT) GST exemption for imported goods and services bought by consumers defies this principle of fairness. A good purchased at an Australian store will be subjected to GST but the same good can be purchased from an international online site and not be subjected to GST. This not only reduces the fairness and integrity of the tax system but damages local retailers and destroys jobs.

The Retail Council is advocating for a zero threshold for the LVT so that all goods and services are treated the same under the GST system, no matter how they are purchased.

The Retail Council is encouraged by the Government's decision in the 2015/16 Budget to remove the LVT for GST on intangibles purchased online, such as video and music downloads. According to Treasury estimates, this is expected to generate an additional $150 million in revenue in the first year of proposed implementation (2017/18). Nevertheless, the Retail Council argues that this needs to be implemented immediately, rather than waiting until 2017/18, and it needs to be extended to goods.

Modelling undertaken by Ernst & Young[17] shows the revenue generated by removing altogether the LVT on goods will be substantially greater than the cost of administration.

[17] Ernst and Young (2013) Levelling the playing field plus 2015 updated figures

This modelling is based on the collection system which involves the GST being collected at the time of purchase of the good and not at the point of importation, as under the current collection system.

The current customs-based system is out-dated and needs to be replaced with a point-of-sale system so that GST is charged to the customer as the sale is being processed. This is the system used for online purchases from Australian GST-registered retailers and it would work exactly the same way for international retailers. International retailers would register as an overseas retailer in the Australian GST system. They would be unable to claim GST credits, since no Australian-based resources were used to execute the sale, but they would be registered as a collector and remitter of GST to the ATO. Big international brands would register for the system as they have a reputational incentive to do so – they wish to be seen as complying with the law. There is also a 'stick' aspect to the system – if a company was not registered in the system then the shipments to Australian customers would be caught in a standard compliance program that would undertake a small number of random checks at the border. As soon as Australian consumers understand that delivery of their goods may be delayed, then they will stop shopping at non-registered retailers.

This point of purchase approach has two key advantages over the current 'at the border' collection approach:

- It is cheaper to implement because every package does not need to be checked and assessed. This means there are no additional resources or infrastructure costs to customs systems arising from changes to the processing of goods that are imported into Australia. Initial modelling of the cost of removing the LVT focused on this expansion of the current system of every parcel being checked at the border. The Low Value Parcel Processing Taskforce, established in 2012, estimated that continuing to rely on an 'at the border' approach, even with some modifications, would cost at least $450 million a year just for the international mail component. This high cost of collection is clearly a barrier to the removal of the LVT but it is one that can be easily overcome if a point of purchase approach is taken instead.
- It is a self-assessment system. Nearly all Australian taxes are now based on voluntary compliance and self-assessment with a system of audit based on the accounting records of the taxpayer and data matching. For example, income tax, company tax, capital gains tax, fringe benefits tax and payroll tax are all self-assessment systems that have an audit program attached. In contrast, full assessment systems, like the current 'at the border' to collecting GST and customs levies has proved to have excessively high administrative costs. These costs are acting as a barrier to removing the LVT.

The table below indicates that under this proposed collection system removing the LVT on goods in 2015/16 will result in a net increase in GST collections of over $1 billion in 2015/16 which will rise to $1.7 billion in 2020/21. These figures are based on the 2013 model developed by Ernst & Young, updated in 2015. This modelling highlights not only the increase in GST revenue but also the increase in domestic retail spending that would result of the GST being charged on all non-exempt goods irrespective of where those goods were purchased.

Table 2: Impact of LVT removal

Financial impact of removal of LVT	2015/16	2020/21
Increase in GST revenue (gross)	$1,072 million	$1,724 million
Increase in ATO collection costs	$37 million	$58 million
Increase in GST revenue to be paid to states (net ATO costs)	$1,035 million	$1,666 million
Increase in domestic retail spending	$6,458 million	$9,667 million

Note that these estimates are for goods only and would be in addition to the expected benefits derived from removing the LVT on intangibles.

Example 2: Administrative complexity of the GST

The *Re:think* discussion paper featured a discussion about a pizza roll, but this is just one example of the many decisions that retailers and the ATO need to have around the GST classification system.

The Retail Council acknowledges that this is in part due to the exemptions in the GST system, and that a full coverage GST would avoid such challenges. Regardless of whether the GST base remains the same or is broadened, a more timely and cost effective approach is needed. Without a full coverage of GST at a specific rate, there will always be 'grey' areas for classification. An example is salads. Salads are GST free as long as they are not marketed as a prepared meal. Since the commencement of the GST back in 2000 the range of salads offerings has increased and salads are now more considered to be a meal rather than a side. Any marketing like signage saying Salad to Go or Lunch to Go can affect the GST rating.

Example 3: Harmonisation of state taxes

One of the advantages of being a large business is the economies of scale that can be delivered by having common operational costs spread across a large businesses. The complexity of the Australian tax system means these economies of scale cannot be fully realised. Businesses with multi-state operations must navigate not only different tax rates by states for payroll tax, stamp duties and land tax – but also different tax base definitions.

COAG has been working towards state tax harmonisation so that there are consistent rules across Australia. But progress has been slow to date. This needs to be accelerated and made a priority to improve the simplicity of the state tax system.

Example 4: Consolidation of state taxes

There is an opportunity in the review of the tax system to reduce complexity in the system by removing the number of taxes, in particular state taxes.

This type of policy approach was used when the GST was originally introduced in 1999, with several state stamp duties being removed on the introduction of the GST. Such a process should be re-examined during this review to try to improve the simplicity of the system.

As identified in the Henry Tax Review process, of the total tax revenue collected by Australian governments in 2006-07, 90 per cent was derived from 10 taxes. These 10 taxes accounted for 95 per cent of Australian government revenue and over 70 per cent of state tax revenue (including 100 per cent of local government tax revenue). Ten per cent of tax revenue in 2006-07 was contributed by the remaining 115 taxes.[18]

[18] Treasury (2008) Architecture of Australia's tax and transfer system

INDIRECT TAX ISSUES

Why is the Retail Council interested in this issue?

Indirect taxes collected by the Australian Government cover a range of goods and services including fuel, alcohol, tobacco, luxury cars, agricultural levies and tariffs. Around two-thirds of indirect tax revenue comes from three taxes – fuel excise, alcohol and tobacco. These taxes usually have two purposes; to raise revenue and to alter behaviours by reducing consumption of these goods. All of these products are sold by some Retail Council members.

The indirect tax system needs to be fair so that revenue raised is closely linked to spending in the same area so that it is the payees of the tax that are also the beneficiaries of the tax revenue.
The indirect tax system needs to find the right balance between achieving social goals without unduly distorting economic activity.

The indirect tax system needs to be simple to implement with complexity kept to a minimum.
The indirect tax system needs to be sustainable, this includes considering whether the multitude of specific excises is appropriate or if some consolidation is possible to improve the sustainability of the system into the future.

The Retail Council has identified examples where the indirect tax system currently fails the fair, growth supporting, simple or sustainable tests.

Example 1: Hypothecating fuel excise for road maintenance and upgrades

Road users, including freight operators, are the payees of the fuel excise which is levied via petrol/diesel purchases. However, this revenue currently goes into general revenue and is not necessarily spent on road maintenance and upgrades. A fairer approach would be to hypothecate revenue raised via the fuel excise towards improving the roads users are travelling on.

Example 2: Complexity of alcohol taxes

The alcohol excise system is currently extremely complex and simplification is needed.
Most alcoholic beverages are subject to excise or excise-equivalent customs duty at one of 16 different excise categories depending on alcohol type, concentration, commercial use, and container size. Wine and some other alcohol products are treated separately and subject to the Wine Equalisation Tax (WET).

Some products face particular complexity and can be impacted by both the WET and excise depending on the method of production. For example, cider that comes from the fermentation of grape juice or the juice of apples or pears is subjected to WET. But when ethyl alcohol is added and or additional flavours and colours the cider becomes subject to excise. This often causes issues with suppliers as the taxing component included in the price for excise is higher than the WET, so it also impacts on the final shelf price.

There is also some inflexibility in the excise system when decanting from a larger keg to a smaller/ medium keg, which will attract a higher excise. The excise paid on the initial larger keg is not actually refundable as the decanting is considered to be manufacturing under the Excise Act and taxable, even though at this point no end sale has been made to the customer. This impedes on innovation in the alcohol market in the retail space which can't compete with hotels and boutique craft brewers.

Finally, the WET producer rebate is part of the Free Trade Agreement with New Zealand. This allows NZ based wine producers to claim the Australian WET producer rebate. This impacts unfavourably on competing Australian producers and is also difficult for the Australian Taxation Office to administer.

COMPLEXITY AND ADMINISTRATION

Why is the Retail Council interested in this issue?

The Retail Council believes significant improvements to the tax system can be made by focusing on simplification. This includes consolidating the number of taxes and reducing the number of exemptions and concessions.

Part of the reason the tax system is so complex is that much of it is made up of amendments and rulings that have been written in an ad hoc way, designed to close perceived loop holes and deal with every conceivable situation.

This has resulted in an unbalanced tax system that in an effort to chase perfect integrity has compromised simplicity.

Despite these efforts to chase integrity at all costs, there are tax payers (both individual and corporate) who spend considerable resources engaged in tax planning activities to legitimately minimise their tax. These resources would be better directed at productive economic activity, thus generating more tax revenue.