Employee Ownership Group

27 April 2009

Mr Rob Heferen
Secretary
AFTS Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

AUSTRALIA'S FUTURE TAX SYSTEM

EMPLOYEE OWNERSHIP AND A MODEL PRO-SAVINGS TAXATION SYSTEM

Dear Mr Heferen,

The Employee Ownership Group (EOG) wishes to make the following further submission to the review of "Australia's Future Tax System". We make this submission in response to *Australia's future tax system: Consultation Paper December 2008.*

In our original submission of 9 December 2008 we sought to focus on:

1. the contribution employee share ownership can make to business productivity, job creation and retention, and workforce satisfaction and commitment; and

2. the obstacles placed by the taxation system in the way of employee share ownership achieving these objectives.

In this submission we wish to take up the theme of employee share plans as an integral part of a future national savings strategy. Our remarks are prompted by the discussion in *Consultation Paper December 2008* on the subject of an expenditure tax and, in particular, this striking observation:

> "Given the mix of taxes in Australia, and the existing concessional tax treatment of some forms of saving, it is possible to characterise the aggregate tax system as providing a mixture of the income and expenditure tax concepts. The issue then is whether to shift this mix further in one direction or the other, if at all." *(AFTS,* December 2008, p.67)

This candid statement points to the unresolved confusion of taxation principles operative within the Australian tax system. The failure to clarify what principles ought to operate has contributed to Australia's development as a low savings, high debt, consumption orientated society. The present review offers an opportunity to break with the muddle that has characterised the evolution of taxation in this country and to set a course toward a tax system that encourages saving and investment rather than debt and consumption.

Our present tax system promotes debt and consumption because of the way it combines high taxation of savings with a concessionally taxed compulsory system of retirement incomes saving. The present regime, while submitted to, is deeply resented in the community because savings are difficult to make outside of the superannuation system and those that are made inside it are locked away until retirement. Given the heavy taxation of savings made outside superannuation, the incentives to accumulate debt rather than savings, to meet short- and medium-term expenditure objectives, is powerful.

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To illustrate the strange anti-savings bias of which the present tax system is capable, one need only look at the way savings are taxed when made via the key employee share plan provided under Division 13A (ITAA). Savings accumulated in this plan - the tax deferred share plan - are subject to *twice* the level of capital gains tax relative to a parcel of investments in equities acquired by ordinary means. In short, the deferred share plan is taxed to minimise savings and to maximise revenue raised.

(The economic consultant Per Capita and the Employee Ownership Group will publish jointly in June 2009 a paper illustrating this point. We request that this paper - *Employee Share Ownership and the Progressive Economic Agenda* - be treated upon publication as an attachment to this submission.)

Australia needs a national savings policy wider in conception than our current system of retirement savings. We need a whole-of-life savings strategy supported by a broad spectrum of savings vehicles, with different savings objectives, all taxed in the same way.

The suite should include at least home savings accounts, employee share ownership plans, and superannuation. The suite might also include an Australian equivalent of the UK's Individual Savings Account (see *Employee Share Ownership in Australia: the future* - Appendix E.)

In *Consultation Paper December 2008* the merits of both 'post-paid' and 'pre-paid' expenditure tax systems are discussed. Either method would be a far superior way to tax all of the above savings instruments than the present unresolved mix of income and expenditure approaches - a punitive regime acutely manifest in the present taxation of employee share plans.

If the AFTS review is, in the end, unable to recommend to Government a clearly pro-savings taxation system based on one or other expenditure tax method applicable to all savings instruments, then it should try to rescue from the accumulated confusion of Australian taxing practices at least one firm principle: that income should be taxed as income and capital gains as capital gains. This would have the merit of creating space for the development of employee share ownership - a development that is both constrained and disfigured by the operations of Division 13A (ITAA) as indicated in our 9 December 2008 submission.

While the Employee Ownership Group would be gratified by such a modest reform, we hope that the opportunity presented by this review will not be lost. Australia's taxation system is much in need of something more than limited fine-tuning. The current global economic and financial crisis has identified as never before the tremendous vulnerability of under saved, highly indebted Australian households. To help transform them into something less fragile, the AFTS review needs to recommend a watershed change to the Australian taxation system - something that will stimulate a new culture of savings and investment supported by a wide variety of savings vehicles taxed in accord with common principles and rates.

Yours sincerely

Gaacarrabe,otti
Group Secretary