Richard J. Tanner

11th February, 2009

AFTS RECEIVED
23 FEB 2009

Australia's Future Tax System Secretariat
The Treasury
Langton Crescent
Parkes ACT 2600

Dear Sirs

Thank you for sending me the full Consultation Paper and Summary together with the Retirement Income Consultation paper. Over the Christmas period I have read these papers and wish to make these further submissions.

You obviously have an enormous task because of the semantics problem with tax reform meaning different things to different people. Your principal task will be to sort out the national interest as opposed to the special interest groups who tend to make the most noise about taxation. You will recall that my submission in October 2008 dealt almost exclusively with what I perceived to be the major problem viz the very steep progression in the personal income tax structure in Australia.

After reading your interim papers, I more firmly than ever hold that view. This submission is designed to show that even the more disparate elements of other submissions can be accommodated if the steep progression problems can be overcome. Over and above these considerations which will be dealt with later is the global economic crisis which in my submission can only be dealt with in Australia with a new approach to personal income tax.

Many reasons have been postulated for the current crisis such as bad lending practices from banks overseas and lax administration on behalf of the regulatory authorities. Very little attention has been paid to the real cause of the problem - the unbridled abuse of the progressive tax system in most countries by politicians and bureaucrats. It would appear that those countries which have flat or flatter personal income tax rates have emerged from the current crisis relatively unscathed.

High personal marginal rates oftax have penalised equity and encouraged debt. Governments around the world now have to deal not only with collapsing personal income tax revenue but also increased spending on social security items such as unemployment benefits and pensions. It is the intention of this submission to show that the personal income taxation policies of all the political parties and the Government will not only exacerbate the existing problems but create yawning Federal Government deficits which will need to be dealt with by increasing not decreasing personal marginal rates.

One of the features of the Consultation Paper is the appalling number of submissions which call not only for the maintenance of the high progressive personal income system but to increase the progressiveness in the system. The excellent definition in Chart 1.2 on Page 24 ofthe distance in kilometres to World GDP should reinforce the notion that Australia should have a low marginal taxing regime to not only deal with the distance to markets but to have a competitive edge in wage levels.

The Progressive Income Tax System with the appropriate acronym the PITS has not succeeded in bringing social equality in Australia and indeed because of the manner of its administration has actually widened the disparity between the so-called rich and the so-called poor. The structure of the PITS has given rise to the widespread use of the partnerships and trusts where predominately family income has been allocated to individuals with lower personal rates. This will be quantified later in an attempt to show the fiscally lethal government revenue games which the irresponsible political parties are playing by pandering to the politics of envy.

If the use of trusts to split income were stopped there would be widespread dislocation in the economy as businesses and families have come to use the system which politicians in the infinite wisdom or folly have put in place.

The explicit Tax Free Threshold (TFT) of $6,000 and the Low Income Tax Offset (LITO) have given the impression that average personal income tax rates at various levels of Average Weekly Earnings (AWE) have fallen over the past twenty five years. Chart 3.3 on Page 56 is in my opinion misleading as the real measure should be marginal tax rates at various multiples of AWE. These was attempted in Schedule 3 of my original submission and shows that marginal tax rates have not fallen and remain at a high plateau since the mid 1960's when politicians discovered the plaything of the PITS. Any reduction in marginal tax rates have been more than taken up with the introduction of the Goods and Services Tax.

Australian politicians are most adept at creating the highest and most frightening marginal tax rates in the industrialised world and then explaining this away by giving tax cuts at election time. Schedule 4 of my original submission is, I believe, an accurate but frightening portrayal of how Australian marginal tax rates where the bulk of personal taxable income resides are the highest in the industrial world and more importantly in the rapidly developing third world, competing with Australia.

The table developed by myself in the original submission was based on figures gleaned from the Ernst & Young Worldwide Tax Surveys in local Australian currency converted by myself at exchange rates ruling at the end of December 2007.

A more accurate portrayal of how competitive Australia's marginal tax rates are would be a survey comparing the AWE at various multiples with marginal tax rates in local currency of that country. This may be an area where Treasury can provide a clear picture.

The central thrust of my original submission was that Australia's high marginal tax rates could only be lowered if the explicit TFT was abolished and the general LITO replaced with a social security credit reflecting the financial circumstances of a genuinely lower income person. Incontrovertible evidence was presented showing that more wealthy elements in the community were legitimately using the TFT and LITO to pay little or no tax. This evidence was based on figures gleaned from the 2005/06 Taxation Statistics from the Australian Taxation Office.

The concerns which I raised in my original submission have only been reinforced by some of the statements and figures in the Consultation Paper. The statement on Page 81 of the Consultation Paper is correct in its simplistic form "A progressive tax system is characterised by average tax rates that rise with income in line with the idea that reductions in income (caused by taxation) can reduce the wellbeing of low income earners more than high income earners. It allows revenue to be collected with lower tax rates for those on lower incomes. In 2005/06 a revenue neutral flat tax would have required a 24% tax rate. This would have resulted in almost 80% of taxpayers paying more tax (those with a taxable income of less than $55,200 in that year.")

It may well be added that the 20% taxpayers earning above $55,200 who would pay less tax under a flat tax regime pay approximately $70.86 billion or 65% of total personal income tax. (Refer to Schedule 1 in my original submission). Flat tax could be justified on these grounds alone but it would be too much for the politics of envy so rampant in Canberra.

However, the tax demagoguery as practiced by all previous and exiting Prime Ministers and Treasurers is about to come to an explosive and unpredictable end. It will come in the form of a collapse in the income tax base and the demands on Government for increased social welfare spending caused by the global economic meltdown.

The seeds of the coming crisis are sown on page 82 of the Consultation Paper under the heading- Interactions Between Personal Tax Rates and Offsets - "The most widely available offset is the LITO (Low Income Tax Offset). It was used by over <u>five</u> <u>million</u> <u>individuals</u> (my emphasis) in respect of the 2006/07 year when it was half its present size."

The LITO in 2006.07 was $600 which grossed up at the first marginal tax rate of 15% gave an effective tax free threshold of $6,000 + $4/000 =$10,000. The LITO in the current year is $1/200 giving an effective tax free threshold of $6/000 + $8/000 =$14/000.

The following statement on Page 82 of the Consultation Paper is at best wrong and at worst a most dangerous simplification of a looming problem. "Increasing the LITO costs less in forgone revenue than increasing the tax free threshold. This is because increases to the LITO do not flow to higher income taxpayers as LITO is currently withdrawn over the range $30/000 to $60/000 income range."

Assuming linearity if over 5 million individuals used it in 2006/07 when the LITO was $600 then 10 million individuals will use it this year. This is 87% oftax filers. The robustness of this alarmingly high figure must be checked against other known information and statistics.

From the Taxation Statistics 2005/06 Table 9/ the one percentile-

At $14,000 ($14/028) is 846,785 taxpayers

At $60,000 ($60/233) is 7A32, 545 taxpayers

The number of taxpayers who will use the LITO

Is	7A32/545
+ Non Taxable Taxpayers	<u>2,102,705</u>
Total	9/535/240

The robustness of the 10 million individuals who will use LITO is therefore confirmed.

The effect on the Taxable Income Base is potentially devastating with the consequent need to raise marginal tax rates. The reduction in the tax base has four elements which need to be examined separately.

1) General Explicit Tax Free Threshold

2) Number of taxpayers to $14/000 becoming Non Taxable Taxpayers

3) Number oftaxpayers overthe range $14,000 to $60/000 who will derive some benefit from LITO

4) The extent to which the effective TFT will be used by higher income taxpayers and businesses

		$ Billion Income Base Not Taxed
1.	There are 11,510,960 tax filers 9,408,255 tax payers 2,102,705 non taxable taxpayers	69.0
2.	There will be 846,785 taxpayers to $14,000 who will become non taxable taxpayers	6.8
3.	The average tax rate is 24% overall which implies $5,000 worth of income will not be taxed over the range $14,000 - $60,000 where there are 6,585,760 taxpayers on marginal rates of 15 & 30%	32.9
4.	There are 1,975,710 taxpayers over $60,000. Taxation Statistics 2005/06 Page 11 show that there were 2,114,426 personal taxpayers using partnership and trust distribution involving $30.1 billion. This implies average distribution of 14,338 which is the effective TFT.	30.1
	Total:	$138.8

There is urgent need for Treasury to quantify the loss of the income tax base which will occur from the operation of the TFT and LITO. If the TFT was increased to $14,000, the loss of the Taxable Base would be $162 Billion but the latest figures which are three years behind the current year show that the loss is not significantly lower at $139 Billion.

Certainly the loss of tax base would mean that the concept of a flat rate of tax above $14,000 would need to be 34%. This is both above the first marginal rate of 15% at $6,001, and 30% over $34,001.

The contraction of the taxable income base is alarming and runs counter to the broad thrust of my submission namely broaden the base but lower the rate.

It will be incumbent on the Treasury Inquiry to fearlessly counter the cant and sophistry of the Australian political parties and their respective Governments and Executives. The PITS cannot provide the answers to Australia's systemic tax problems and has demonstrably failed to be efficient, equitable and transparent to reduce complexity. Future generations will legitimately ask why this intolerable state of affairs was allowed to happen unless impartial members of the current panel give an unbiased assessment ofthe current personal income tax arrangements in Australia.

It is my submission that the current arrangements, if allowed to continue, will cause the same type of economic havoc that has beset the world financial markets over the last year. Indeed, I will go further and say that the PITS has been the root cause of the financial market chaos and economic history when it is recorded, will show that this is the case.

I will attempt to answer the various consultation questions to fill in the detail of how a low flat rate of personal inco e tax can solve the inherit problems in the system.

Yours faithfully

Richard J. Tanner

Australia's Future Tax System

Answers to Consultation Questions

By Richard J Tanner

11th February, 2009

Contents

It is my submission that all the objectives and scope ofthe inquiry as outlined in Appendix A can only be achieved by adherence to the broad principle of a low flat rate of personal income tax.

Question 1.1

Broadly speaking all income from whatever source should be taxed at a low flat rate of 15%. This is the current rate which roughly divides the bottom half of taxpayers from the top half. It is therefore the median rate which can be extended to average weekly earnings where for political and revenue reasons a 30% rate should be struck.

Income would be defined as personal exertion income, fringe benefit income, allowances, current salary sacrifice, income for superannuation purposes and capital items.

All social security payments would be grossed up by 18% to take into account that all pensions would be taxed at source by 15% and all pension recipients would be required to submit a tax return.

All withdrawal rates (tapers) on all pensions would be reduced to 15% so that all pension income would be subject to an effective marginal tax of no more than 30%. Rebates could be given to all social security recipients so as to preserve, if necessary, the current tax free nature of their pension.

Question 2.2

Yes, provided the system as outlined in 1.1 is introduced there would be: -

i) An explosion in employment
ii) Amelioration of wage demands
iii) An explosion in investment
iv) Less need for social security payments
v) An increase in Government revenue not only from personal tax collections but also GST revenue
vi) The individual would be secure in the knowledge that he or she could keep at least 70% of earnings and most cases 85%.
vii) Young families with mortgages could more easily deal with debt obligations particularly after the birth of children

Question 3.1

The problems are not with the overall mix of taxes in Australia but the individual negative features of various taxes.

i) Business and Income - it is easy to split income by way of trusts and partnerships into areas where there is not tax or low marginal rates. The system outlined in the answer to Question 1.1 would abolish this benefit.
ii) Labour Income - the worst feature of the current high marginal taxing systems is the legitimacy it conveys on high pre tax wage demands.
iii) Consumption - the worst feature of the consumption taxes is the regressive nature of them with the burden falling disproportionately on the lower income group.

iv) Transactions and Assets - if a low flat rate of tax could be introduced, there would be no need for the 50% abatement of capital gain and there could even be sensible discussion of whether the family home should be subject to a low flat rate of tax.

Means tests should apply to overall level of income from whatever source as defined in answer to Question 1.1.

Question 3.2

The current system does penalise the returns to savings in two ways. Firstly, the quantum available for savings is only available after the payment of marginal rates which are exceedingly high by world standards. Secondly, debt used to acquire assets attracts a taxation deduction equivalent to the individuals' marginal tax rate. Under a system outlined in Questions 1.1 and 3.1 there would be more equity available to savings and less deduction for debt. There would be no need to change the structure oftaxes and the means test as the existing problems would be self correcting.

Question 3.3

Under the existing convoluted system the tax transfer system does deal with property and wealth in an appropriate manner but it does so in a most unequal way. The highly progressive personal income tax rates on personal exertion income precludes the sensible discussion of whether the most important property asset - namely the family home, should be taxed on disposal or death.

If a system as outlined in Questions 1.1 and 3.1 could be introduced there could be sensible discussion as to whether the family home could be taxed on disposal or death at a low flat rate. For political reasons this may be at a lower rate than the 15% suggested.

Question 3.4

My inbuilt bias against consumption taxes is based on the fact that they are regressive with the burden placed disproportionately on the lower income groups. My strong view is that attempts should be made to straighten out the shemozzle in the personal income tax mess before the role of consumption taxes is charged.

Question 3.5

The short answer as to whether greater application of user charges should be made is definitely no. The reason for this is that user charges such as road transport charges feed directly into the cost of goods. This is especially true in Australia with its vast distances pushing up the cost of transport in moving goods and livestock to and from markets.

The funding of Government services to bring about social, environmental and economic benefits should be done so from general revenue whose principal source is personal income tax. This general revenue sources should be from a low flat rate of personal income tax.

Question 4.1

The general answer to this complex question is to discuss what is termed vertical, horizontal and intergenerational equity.

Vertical equity is about the capacity to pay. There is universal agreement about the notion that the more one earns, the more one should pay tax. The academic argument is whether one should pay progressively more tax or proportionately more tax.

The Progressive Income Tax System (the PITS) has degenerated into a shemozzle with the cash economy and legitimate income splitting rife, to say nothing ofthe highly dangerous implications for Australia's trading position in the world. The PITS has been abused by politicians and governments of all persuasions and provides endless opportunity for chicanery. It should be immediately abolished.

Horizontal Equity loosely defined means taxing all income at the same rate. Because of the PITS various types of income are not taxed equally and indeed some forms are not taxed at all. For instance, fringe benefit are not taxed at all in the employees hands, allowances are not taxed, housing is not taxed, dividends in the hands of individual are largely tax free or rebated at the corporate tax rate of 30%, and superannuation income is not taxed if paid from a taxed superfund. By abolishing the PITS all income from whatever source can be taxed at a low flat rate.

Intergenerational Equity revolves around the changing financial needs over a lifetime. Young people do not need much income but they should be encouraged to save for the financial demands of children later in life. Older people do not need as much income except for medical reasons but believe their income should be at lower rates because they have paid high marginal tax rates throughout their working life. Because ofthe PITS there is intergenerational resentment.

As I stated in my answer to Question 1.1, the personal tax system can only be changed to achieve the goals of greater simplicity, transparency, equity and efficiency if the PITS is immediately abolished.

It is worth repeating the opening lines of my original submission -

"Stripped of all the hyperbole bunkum and buffoonery in the tax reform debate the quintessential question which should be asked is "Should the higher part of your income be taxed as a higher rate than the lower part?""

I note with alarm that the key message from a number of submissions is that there should be greater progressivity in the personal tax system through higher rates for higher income earners. This is the most important issue which the panel must address. If the PITS is abolished all questions and issues can be sensible addressed and a fairer system put in place.

Question 4.2

Please refer to Schedule 1 of my original submission together with Schedules 2 & 7.

Whilst I have railed against the PITS, the appropriate distribution of income tax will not change under the proposal to abolish the TFT and general LITO and replace it with a low flat rate system of 15% up to average weekly earnings (AWE) with a marginal rate of 30% above AWE.

It should be pointed out that the lower income earners fall into the following categories: -

1) Juniors entering the work force for the first time
2) Older people leaving the work force for the last time
3) Wealthy people negatively gearing their income
4) Part time workers
5) Part year workers
6) People travelling overseas for part or all of the year

They will not be disadvantaged by paying 15% from the first dollar up. Indeed existing taxpayers have the TFT pro rated according to the time of the year worked and suffer much higher Pay As You Go rates (PAYG) if moving to a second job as indicated in the Taxation Departments - weekly or fortnightly tax (PAYG) deductions for second jobs. Further, my Schedule 7 shows the very high average tax rates for these taxpayers earning less than $6,000.

My proposal for a top marginal rate of 30% will result in a distribution of taxpayers almost identical with the present distribution. The top five percentile average rate of tax of 38.2% is overstated by as much as 6 percentage points due to the highly misleading arrangements of including franking credits in both net tax paid and taxable income.

Furthermore under my proposal all income including fringe benefits, allowances and salary sacrifice through superannuation will be included in a higher income person's taxable income resulting in them paying more tax not less. Income splitting will be effectively eliminated.

All thresholds should be immediately abolished and not indexed with a low flat rate of tax of 15% (the current median rate) there will be no need. Schedule 7 of my original submission shows that distributions over time (age) will not change.

Question 4.3

The current personal income tax base is in aggregate fair under the current chaotic and torturous conditions of the PITS. Under a low flat rate system it would be redefined to include all income from personal exertion, fringe benefits, allowances, salary sacrifice through superannuation and capital.

Deductions under the PITS should remain as there would be widespread dislocation, disruption and financial hardship if they were abolished. Under a low flat rate system of 15% the value of deductions would fall dramatically.

Question 4.4

Under the low flat rate of 15%, all pension payments would be taxed at 15% on a grossed up pension payment of 118%. The notional 15% would be deducted at source so pension payments would be the same as present, with the recipient unaware that he or she was paying tax. All additional income by the social security recipient would be taxed at 15% but the recipient would be given six months after the lodging of compulsory annual tax return to pay the withdrawal or taper tax of 15%. Fine tuning tax credits could be given to maintain a fixed level of income from the total of social security benefits and any other personal exertion income.

Question 4.5

Generally people in different circumstances should not be taxed at different rates at source and this should apply for occupation and location.

In respect of age there could be a tax offset to apply upon the lodgement of an annual tax return. The justification for an age tax offset would be that these people have paid high marginal tax rates throughout their working life.

Location offsets should be discouraged as taxpayers will give hardship addresses. This area can best be addressed by granting freight subsidies for the transport of goods and services to outback locations.

Tax offsets rather than deductions are the best way to achieve differential taxation. These would be standardised with the introduction of a low flat rate system.

Question 4.6

All fringe benefits should be taxed in the hands of employees rather than employers. Employers and companies suffer enormous amounts oftime and money administering the current chaotic arrangements.

The one group of fringe benefit recipients to whom this problem would be decided are the parliamentarians themselves. Perhaps they could be given a non taxable lump sum each year to cover travel and the running of electorate offices.

Question 4.7

Under a low flat rate of the system as outlined, income tests could be abolished. All social security payments grossed up by 18% and taxed at 15% at source would still be made. Each year other income would cause a 15% taper tax to be applied which would need to be paid along with other income tax within six months of the tax filer submitting a compulsory tax return.

Question 4.8

Objectives such as family assistance and poverty alleviation should be paid on a needs basis much the same as it is now with the Family Tax Benefit Part A and Part B to low income one earner families and single parent families. It is noted that the taper rate on these payments was reduced in 2004 to 20%.

Under a low flat rate tax system the taper rate along with all other taper rates could be reduced to 15%. The major feature of a low flat rate tax system of 15% to AWE and 30% thereafter is the breaking of the nexus of high marginal tax rates and the demand by higher income taxpayers for the return of tax through Family Tax Benefits. At present for political reasons this cannot happen and so "Churn" occurs.

Question 4.9

There is one feature of the current tax arrangements with the explicit TFT and LITO together with the high marginal tax rates is the pressure from a financial prospective for the wife to return to the work force as soon as possible following the birth of a child when a woman's hormones are naturally in disarray. The husband is taxed at higher marginal rates but the woman can earn tax free amounts even though she may be exhausted and tired. Whether a woman should make an early return after the birth of a child to the workforce is a family matter and should neither be encouraged or discouraged by tax considerations.

The current high marginal tax arrangements create problems for the duration of income support, costs of work and searching for jobs, costs of children and the value of home production. These are family matters which should be dealt with by a low flat (constant marginal) rate and not by the state attempting to lay down standards which will vary widely from household to household.

Question 4.10

The only common benchmark for transfer payment should be one of needs. Different people in different circumstances have widely different financial requirements. The current system starts out on the premise that everyone is a pauper when latently this is not so. The explicit TFT and LITO are being legitimately used by the higher income earners to offset the ravaging effect of a high marginal taxing system.

Any indexation arrangements for transfer payments should be linked to the consumer price index.

All indexation arrangement for various tax thresholds should be abolished.

Question 4.11

No. With a low flat rate of tax of 15% and 30% above AWE many transfer payments to people of working age can be abolished. For instance, the cost of the child care rebate $344 m and the baby bonus tax offset of $176m - total of $0.5 billion should be viewed against the rapacious plunder of the PITS bringing in approximately $127 billion this year.

Question 4.12

The central thrust of a targeted system should be to reduce effective marginal tax rates to as low as possible. The positive marginal tax rates of 15% will encourage more people to take on extra work eliminating the low income trap.

Also, negative marginal tax rates of 15% (tapers) at the bottom ofthe income scale will encourage people to find work, lowering the unemployment trap.

I see no reason why effective marginal tax rates need be higher than 30% for the vast majority of taxpayers. Low income workers would be secure in the knowledge that they could engage in any amount of work and still keep at least 70% oftheir combined earnings and pensions. This compares with effective marginal tax rates as high as 80% at present. Strict eligibility requirements would still apply.

Question 4.13

The non taxable nature of allowances could be abolished as well as the "free areas". The taper rates for all income should be reduced to 15%. This includes Pensions (currently 40%), Newstart (60%) and Family Tax Benefit (20%). This would accommodate the increasing diversity of work and the greater incidence of part time work. With a low taper rate on all pensions and allowances there would not be the need for incentives to be targeted.

Question 4.14

The answer to this question is similar to 4.12. A new low flat rate of tax of 15% will encourage people to take on new skills which presumably would mean higher wages. Reduction in the taper rates to 15% would allow people to more easily take on the costs of acquiring these new skills.

Question 4.15

If an effective marginal taxing system of 30% (15% positive and 15% negative) could be introduced, consideration could be given for abolishing the means and assets tests. There would simply be a requirement for the withdrawal or taper tax of 15% on all pensions and allowances to be paid within six months of a tax filer submitting a compulsory tax return.

Question 4.15

The unit of assessment for tax and transfer should continue to be the individual not a combined husband and wife return. The high incidence of divorce creates a bureaucratic nightmare for the Tax and Social Security Departments.

Income definition should include all personal exertion income, allowances, fringe benefits and salary sacrifice for superannuation payments.

The period of assessment should be yearly with the requirement to pay taper tax within six months of the filing of a compulsory tax return.

Assets and Income Tests could be abolished under a policy of a maximum effective marginal tax rate of 30%.

Question 5.1

One of the most deleterious effects of the PITS has been that high marginal tax rates throughout a persons' working life has in a significant number of cases left the individual with insufficient money for retirement. If a low flat rate system of 15% up to AWE and 30% thereafter could be introduced should there be sufficient income to allow the individual to provide for his or her retirement.

One initiative which should be investigated is the compulsory contribution by the individual of 6% of his total or taxable income into a superfund. This would make the total contribution of 9% by the employee and 6% by the individual to bring the total contribution to 15 % which is generally recognised as the standard benchmark necessary.

The Age Pension will always be necessary and this can be augmented by reducing the taper rate from 40% to 15%.

Question 5.2

There is some doubt from an actuarial point of view whether the 9% contribution rate by employers will be adequate. As outlined in Question 5.1, it would be necessary under the new low marginal tax regime for the individual to contribute 6%. At present individuals on $30,342 or less can make personal contributions of $1,000 (3%) with the Government Co-contribution of $1,500. This system could be expanded for the self employed, individual with broken work patterns, such as carers, women and migrants.

Question 5.3

The accepted benchmarks of either indexing the aged pension to the Consumer Price Index or to a benchmark of 25% of male total earnings is considered to be appropriate and adequate. The major component of adequacy is whether an aged pensioner has paid offthe home, whether it is still mortgaged or whether the aged pensioner is paying rent. Special considerations will need to be given to individuals in these situations.

Question 5.4

The role of government is assisting individuals to meet their retirement income expectations is to stop plundering personal exertion income during their working life at the highest marginal tax rates in the world.

With a low flat rate of personal income tax there can be a more rational approach to all aspects of retirement policy.

The role of government as individuals' income increases over their working lifer should be limited to providing a safety net for those individuals who do not have sufficient for retirement and to guard against the collapse of markets and companies who have been managing retirement and superannuation monies.

Question 5.5

It can be argued that a small minority of high income earners receive a disproportionate benefit especially in the area of salary sacrifice into superannuation. Some industry surveys quote that 5% of individuals receive 37% of the benefit of tax concessions.

With a low flat rate of tax of 15% to AWE and 30% thereafter to apply to all fringe benefits and salary sacrifice this distortion will substantially be rectified. This new tax regime will allow a much smoother transition for individuals from working to retirement.

Question 5.6

The answer to this question is similar to Question 5.5. With the abolition of the PITS you should be able to abolish the 15% contribution tax for lower income earners. The level at which this could occur would depend on actuarially studies and yardsticks incorporated into the aged pension.

Question 5.7

The age limits for accessing superannuation and eligibility for the age pension should remain the same. The key question is what incentives should be given for older Australians to remain in the workplace. The most important incentive is to reduce the aged pension taper rate from 40% to15% thereby encouraging older Australians to seek work but secure in the knowledge that they will always have the base aged pension.

Question 5.8

The collapse of stock markets around the world and the unbridled chaos in the credit markets have come as a stark warning that the current investment models are unsatisfactory and not guaranteed. The compulsory contributions by employers have reduced income to employees and then handed over to fund managers who in turn farm out the funds to other managers in the form of hedge funds, balanced funds and other funds whose activities defy description. Many of these funds have had redemptions frozen.

Whilst there has been a seemingly never ending stream of funds into the stock market, there must now be a realisation that a policy of compulsory superannuation levies being used to finance the extravagant lifestyles of fund managers is not the most desirable.

The panel should investigate a more rational scheme whereby superannuation funds can be invested part in government infrastructure bonds albeit with more modest returns.

Question 5.9

The complexity is primarily due to the proportions of taxable and tax free superannuation when the pensions started. Taxable super is that which has been concessionally taxed during the accumulation stage, either as a contribution or as investment earnings. Tax free super is generally personal super contributions for which no tax concessions have been claimed.

Most lower income groups with relatively small superannuation get rid ofthe lump sum and go on the aged pension.

The issue which will require some research is how the lump sums can be converted and integrated into the aged pension without going down the annuity route.

Question 5.10

This question has been partially answered in other questions. The broad thrust is to use the age pension as a supplement for other investment income and/or personal exertion income in retirement. This can best be done by lowering the withdrawal rates from 40% to 15%.

The means test could be abolished by everyone receiving the age pension but a strict retirement of the individual to give up $1 of pension for between every $6 to $7 of all other income -the 15% taper.

Question 5.11

The major factor affecting workforce participation for older workers is the very high withdrawal rate for pensions of 40% over and above the "free" area.

The means test supposedly reduces the overall cost of the age pension but its presence increases effective marginal tax rates which affects individual decisions to work and save.

The younger generation have to cope with the highest marginal tax arrangements in the world. They react by saying that they want their taxes back on reaching retirement regardless of their needs. By abolishing the PITS and putting everybody on a lower flat rate this nexus will have been broken.

Question 5.12

If financial intermediation refers to the stability of the banks and other financial houses this should be left to the Prudential Regulation Authority.

Question 5.13

No. Both the Health and Superannuation sectors are big enough shemozzles in themselves without further complicating either situation by integrating them.

Question 6.1

The easiest and least complicated way is to lower company tax. The Income Tax Statistics for 2005/06 (the latest available) shows that all companies overall made a taxable profit of $191 billion and paid $47.8 billion in tax giving an overall tax rate of 25% against the nominal tax rate of 30%. Prima facie the corporate tax rate of 30% could be reduced to 25% without effecting tax revenue. However effective average tax rates are traditionally 5% point below the normal rate.

With a lower corporate tax rate there is less incentive for transfer pricing by paying for trademarks or patents or invoicing goods to countries where there is a low corporate tax rate.

Lower corporate tax rates should encourage foreign investment in Australia which is needed to balance our lamentable current account deficit.

Question 6.2

The taxation of all fringe benefits by the individual rather than by the company at the grossed up top personal marginal tax rate would be the single most important cost saving to companies not only in money but also in time. It should also pointed out that a company tax rate of say 20% would mean that fully franked dividends would only pass through to individuals at 20% rather than 30%.

Question 6.3

Corporate tax rates tend to be passed on into the general economy as a cost to the goods and services produced. A lower corporate tax rate of 20% will lessen the costs to the general community.

Matters raised in Questions 6.1 and 6.2 will minimise operating costs and encourage entrepreneurial activity.

Question 6.4

The basis for capital grains in Australia between individuals and companies should be the same. With the changes suggested for personal income tax to include terms of capital there should be no bias against companies.

Question 6.5

A lower company tax rate will provide a bias in favour of equity and lessen the deduction for debt. Recent corporate collapse should require a bias in favour of equity over debt.

Question 6.6

There should be no differences between small business and other larger businesses as there would always be a definitional problem. The attention to matters outlined in Questions 6.1 & 6.2 would be of most benefit to small business. High and legitimate pre tax wage demands by individuals working for a company is usually the greatest cost to a company or any small business. By adopting a low flat rate personal income tax regime the pre tax wage demands will be reduced with benefits to small businesses.

Question 6.7

A lower corporate tax rate will mean that the value of dividend imputations will only flow through to individuals at the corporate rate, thereby giving a more neutral tax treatment to other forms of household savings such as deposits.

Question 7.1

The appropriate tax treatment for Not for Profit (NFP) organisations should be based on the High Court interpretation i.e. a commercial business may be a charity if its profits are required by its constitution to be given a charity.

Any cost advantage that a NFP organisation has in respect of Fringe Benefit Tax (FBT) will be neutered by the requirement of the individual to pay FBT.

Question 7.2

No. Even with the imperfections of the existing system it is preferable to the Government by whatever decision making process directly funding NFP organisations.

One aspect of the removal of the PITS and its replacement by a low flat rate of tax is the lessening of the value of the tax deduction for the individual when contributing to a charity.

Question 8.1

The personal income tax collections at approximately $127 billion are by far the most important and therefore reform should be based on this area. The cost ofthe PITS is particularly severe on low income groups who use the services of the professional sector. The professional sector uses pre-tax considerations in setting their fees. No more so is this evident as in the medical, legal and accounting professions.

By abolishing the PITS many costs will be dramatically reduced and the system made simpler.

Question 8.2

Anyone who thinks that personal income tax returns can be simplified under the PITS is dreaming and suffering delusions.

There is a dangerous direction for income tax policy in Australia for people to become Non Taxable Taxpayers. Already they number over 2.1 million and with the planned increases in the LITO to $1,500 in 2010/2011 the effective tax free threshold will rise to $16,000 causing a potential $184 billion of personal income not to be taxed or be available for legitimate income splitting. Any hope of reductions in the marginal tax rates will simply be not available unless Government resorts to running large deficits.

The process of simplifying personal income tax returns can best be achieved by abolishing the PITS. The policy of removing the requirement for some taxpayers to lodge returns should be resisted as there has been an alarming increase in the category of non taxable taxpayers. With the effective tax free threshold set to increase to $16,000 by 2010/11 there will be many more than the existing 2.1 million non taxable taxpayers.

Every citizen in Australia should be required to submit an annual tax return including those on social security. The tax return can be used as a starting point for the payment of social security on a needs basis with a much lower 15% taper on all pensions.

The Tax Department and Department of Social Security could even be amalgamated.

Question 8.3

With the abolition of the PITS and its replacement with a low flat rate of tax the system will become simpler. The system will by definition become more efficient and more equitable. There will be no need for these two elements to be traded off for simplicity.

Question 8.4

Complexity, uncertainty and cost will be reduced and in the process the transparency, understanding and support for the system will be embraced by a great majority. There is urgent need to stop politicians of all complexions abusing the PITS by buying off of individual groups and giving tax cuts at election time whilst between selections using the PITS to engage in the plunder ofthe individuals income at the highest marginal tax rates in the world.

Taxes and transfers in Australia are most complex because the tax system is being combined with social security. These two vitally important functions should not be cross collateralised. The Tax system should be simply a revenue raising function and the social security system should be to look after those in less fortunate circumstances for whatever reason. The more complex a tax system the more it will be legitimately abused by taxpayers especially higher income taxpayers.

With the abolition of the PITS and its replacement with a low flat rate system and low 15% taper on all pensions, all the elements of complexity, uncertainty, cost, transparency, understanding and support for the tax system will be improved.

The attitude of most people at present in the light of the obvious unfairness in the system is to use as many loopholes as possible to reduce their tax liability. The spectre of the Australian Tax System falling into disrepute is very serious for all.

Question 9.1

Revenue raising functions should primarily be a Federal Tax matter. Inter-government transfers are a spending function and should be outside the terms of reference for the inquiry. The panel should pay strict attention to the imperfections in the existing Taxation or revenue raising system and leave the spending function to another inquiry.

It should be noted however that if the personal income tax system could be improved along the lines suggested there will be great scope for reductions in Government spending and redirection to the areas where the need is great.

Question 9.2

Given the broad range of State Taxes it would be nearly impossible to dictate to the States which taxes should be abolished in return for a greater share of the Federal Tax Pie which raises most of its taxes through personal income tax.

The prospect of States setting their own income tax thresholds and rates is a most tantalising prospect. This has only ever been attempted in Australia once in Queensland in the 1980's by the Premier, Sir Joh Bjelke Peterson. The politics were most interesting.

Local Government should be given a fixed percentage of the tax pie. Allocations to Councils would be difficult in areas of vast size and remoteness.

User charge taxes should be discouraged as they feed into costs for the whole economy e.g. the road user charge which in Australia with its vastness and remoteness to markets especially feeds into food costs.

Question 9.3

State Governments should generally stay out of the area of income redistribution. Given the mess that Federal Governments have made out of income redistribution there is no evidence to suggest that State Governments would do any better and in all probability make the existing shemozzle even worse ifthat were conceivably possible.

Question 9.4

This has been explored thoroughly in Question 8.

Question 10.1

The existence of the PITS precludes any sensible discussion of the tax transfer system in respect of housing. The reality is that no politician would be game to tax the sale or transfer on death of the matrimonial home under the present regime. If however a low flat rate tax could be introduced it would be politically possible to tax housing on its sale or transfer as long as the cost base was indexed. Taxing imputed rent would be politically impossible.

The PITS also confers a much higher deduction for interest (so called negative gearing). It should not be abolished as it supports the provision of affordable housing where rents would rise in its absence. Its value would fall with a low flat rate of personal tax.

Government policy should concentrate on a flow of stock suitable for low income public tenants especially for those who have been unable to save sufficiently for their retirement.

Question 10.2

Similar to 10.1. The single most important contribution to housing affordability is to abolish the PITS so that individuals in their working life would have more cash to build up their house equity.

By taxing the sale or transfer on death of the matrimonial home at a low flat rate perhaps at no more than 10% after indexing the cost base, Governments could apply this extra revenue to increase the supply of stock for low income rental.

Question 10.3

If the PITS could be abolished and replaced with a low flat rate of personal exertion income tax it may be politically possible to impose a land tax on all residential properties. As Land Tax is a State responsibility there would need to be some new Federal/State agreement.

Question 11.1

It is appropriate to use taxes on specific goods and / or services to influence consumption choices. The general principle that should be applied is that those specific goods deemed to cause harm should be taxed in a manner where the least harm goods are not taxed. For instance, low alcohol beer should not be taxed at all.

Question 11.2

Probably not due to the highly complex nature of the problem.

Again a system of exempting low alcohol beer from any excise would appear to achieve social objectives.

Question 11.3

The current policy of raising tobacco excise in line with CPI would appear to be the most appropriate. Any substantial increase in tobacco excise would probably see an increase in smuggling from abroad and the illicit trade.

Question 11.4

Duty free concessions for passenger importation of alcohol and tobacco could be abolished.

Question 11.5

Taxation on so called luxury goods should be discouraged. There is always a definitional problem of what constitutes a "luxury" item and quite often a lower income individual needs a "luxury" item. The progressive tax system has utterly failed to bring about social equilibrium and therefore this principle whether it applies to income or goods should be discouraged.

Question 11.6

The general principle that should be applied to cars is one of fuel efficiency and environment benefit. Those cars which are the most fuel efficient should be taxed at the GST rate and those that are fuel inefficient should be taxed over and above GST at a rate reflecting their inefficiency.

Question 12.1

The general principle that should be applied to motor vehicle taxes and road funding arrangements is one of efficiency per ton kilometre. The introduction and widespread use of road trains and B-doubles in the vast rural areas of Australia have contributed to cost reduction per unit of what would otherwise been the case.

Question 12.2

The general principle that should apply is not the fuel taxes but the efficiency of the engines that use fuel. General government tax revenue should be made available to allow highways, roads and bridges to be upgraded to allow the most efficient use of fuel.

Question 12.3

Road user charges should generally be discouraged in Australia due to its vast distances. Government spending on roads would be a more effective way of allowing fuel to be used more efficiently.

Question 13.1

No new taxes such as the Carbon Pollution Reduction Scheme should be effected until a Royal Commission is established to answer the question "Is Mankind Activities Contributing to Climate Change or Is Climate Change a Matter Over Which Mankind Has No Influence?".

The purpose of a Royal Commission is to get to the truth and involves: -

a) Compelling witnesses to attend
b) Compelling witnesses to bring papers
c) Strict rules of evidence
d) The threat of gaol if lies are told

Question 13.2

The most efficient manner which tax transfers can be applied to bring about environmental outcomes is for Governments to build efficient public transport systems in urban areas so that vehicular traffic is curbed. In rural areas there is little of any scope for public transport and the Government should be concentrate on more efficient road systems.

Question 13.3

Great care should be exhibited in the way that tax transfer policies can reshape the environment. For instance, tax concessions currently apply to take agricultural land out of production to grow trees. A forage crop such as lucerne is some 15 times more efficient in removing carbon dioxide from the atmosphere yet it and similar forage crops are excluded from these tax / transfer arrangements under the Kyoto protocol.

Question 14.1

Rent Resources Taxes should generally be discouraged as they lessen the exploration dollars available in offshore locations for oil. It is critical that Australia discover more oil given its chronic balance of payments and current account deficits.

Ad valorem royalties should also be discouraged as they take no account of whether a project is economically viable. Metal prices are notoriously volatile and ad valorem royalties can help make a mining project non viable when metal prices fall. A mine closure can have devastating consequences for people and towns which grow up around mining operations causing loss oftax revenues.

Question 14.2

Similar to 14.1. Charges for Australia's non renewable resources should only be made when there is a strong case for a mineral to be retained for use in the future. The tax dividend should be taken in the form of personal income tax taken out of employees' wages and GST on supplies. In this manner Australia can be globally competitive for mining investment.

Question 14.3

The tax system generally should not be used to ensure that renewable resources are used sustainably.

Sustainable yields from forest are best determined by non tax means and fisheries are sustained by ensuring an adequacy of young breeding stock and controlling net sizes.

Richard J Tanner

11th February, 2009