



Submission to the *Australia's future tax system review*

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1 | Introduction

UnitingJustice Australia, the justice and advocacy unit of the Uniting Church in Australia National Assembly, welcomes this opportunity to contribute to this comprehensive review of the Australian tax and transfer system. This submission furthers the contribution offered in the Uniting Church in Australia's submission to the first stage of this review.

Our responses to the issues raised in the review's Consultation Paper are based on the Uniting Church's belief that taxation is a profoundly moral matter. It is the primary means for ensuring the equitable distribution of wealth and the raising of public money, our "common wealth", in order that we may ensure that basic needs of people in society are met. In other words, it is one of the most important tools at our disposal for achieving economic justice and is vital to a flourishing society.

In its 1988 discussion paper entitled *Economic Justice – the Equitable Distribution of Wealth*,¹ the Uniting Church articulated the following principles which underlie our submissions to the *Australia's future tax system* review two decades later:

- For Christians, the question of economic justice is the question of how we respond to God's free gifts.
- Genuine wealth is not defined in monetary terms, but as those things which contribute to the well-being of humankind.
- There are a variety of ways in which people contribute to society. Production is a communal activity.
- Genuine material wealth is neither money, or luxurious goods and services. Humankind will be genuinely materially wealthy when everyone has access to the following goods and services at the level required to satisfy basic human needs – appropriate food, clothing and healthcare; safe and secure housing; meaningful work, education, rest and enjoyment; and the opportunity to participate in and contribute to communities.
- Access to genuine wealth cannot be restricted to a privileged section of society, for such wealth is a gift from God.
- The Uniting Church has a role to play in the economic policy debate, in helping society reflect on the nature of genuine wealth, especially the gift of the world and the communal nature of so much of the wealth which enriches human life.

About taxation in particular, the Uniting Church believes²:

- Taxation is necessary if the government is to fulfil its responsibilities in provision of services ensuring that all people in the community have their basic

¹ *Economic Justice – the Equitable Distribution of Wealth*, Assembly Social Responsibility and Justice Committee, adopted for church-wide distribution and study by the 1988 Assembly, available at http://www.unitingjustice.org.au/images/pdfs/issues/economic-justice/discussionpapers/economicjustice_88.pdf

² *ibid.*

needs met (a matter of human rights) and correcting the inequitable distribution of income and access to goods, services and resources which results when distribution is left to the private sector and market mechanisms.

- It is how people contribute, according to their means, to the well-being of the whole community, through redistribution and the provision of goods and services.
- When people argue about taxation, they are actually arguing about the level of responsibility they should accept for the community.
- The government has a responsibility to protect the human rights of all Australians. This includes their economic, political and social rights. This requires the horizontal and vertical redistribution of income which is only possible through taxation.

We are grateful for the opportunity to contribute to this important consultation process. We offer this submission as a positive expression of the Uniting Church's commitment to the long-term well-being of all Australians, in particular those who are most in need in our society.

This submission outlines the key principles which we believe should be the basis for a reformed tax and transfer system. It does not address all sections or questions of the Consultation Paper, rather it will address the areas where we feel best positioned to offer comment.

2 | Recommendations

UnitingJustice Australia recommends to the Review Committee that:

- the central design principle of a reformed progressive taxation system be the capacity to raise enough revenue to meet the democratic demands for government expenditure
- the following guiding principles underpin Australia's tax and transfer system
 - it must be designed reflecting an holistic and sustainable understanding of human progress
 - equity must be the first priority
 - people matter – especially those who are disadvantaged and vulnerable
 - tax rates need to be set at a level that ensures governments have the capacity to meet community expectations about services, income support and national infrastructure
 - simplicity and efficiency are important but must be balanced against equity
 - taxation system reform should contribute to reducing the regulatory burden and increasing the transparency of government support
 - not-for-profit community sector services must be supported as essential to the economic and social life of Australia
- the taxation system be re-structured to
 - encourage sustainable and ethical economic activity
 - facilitate individual and community wellbeing and inclusion
 - discourage activities that exacerbate social and economic disadvantage and vulnerability
- politicians and government bureaucrats refrain from using the language of 'burden' in relation to taxation
- socially beneficial personal and family circumstances, such as the raising of children and caring for a disabled, sick or elderly relative require additional support through the tax and transfer system
- the 'ability-to-pay' principle apply in relation to income received by all Australians, regardless of their age or the source of their income
- the corporate tax rate not be reduced
- consumption taxes be structured so that revenue is allocated to programs and services aimed to reduce the prevalence of personally and socially-destructive behaviours
- the application of user charges be based on the principle that people should not be charged for public goods that are necessary for health, safety and an adequate standard of living

- where user charges are applied to change behaviour, appropriate alternatives be in place to enable everyone to choose the lower cost or more environmentally-friendly (for example) option
- effective marginal tax rates be reformed so that no person faces an EMTR higher than the top marginal rate
- a strengthened version of Family Tax Benefit A and a government-funded parental leave scheme replace Family Tax Benefit B, the Dependent Spouse Rebate and the Baby Bonus
- the Newstart Allowance be substantially increased and indexed in the same manner as pensions
- incentives to save be targeted at low-income earners
- the current system of superannuation concessions be reformed so that the benefits are redirected towards low-income earners
 - contributions should be taxed in the same manner as other remuneration and a credit or co-contribution could then be applied
 - the pension income test should be abolished or replaced in favour of a more equitable system for retirement income
- a new top marginal tax rate be imposed on very high income earners
- the current system of tax expenditures be reformed
 - expenditures must provide more benefit to low-income earners than high-income earners
 - government transparency must be improved
 - a clear policy of justification for each expenditure, in accordance with community priorities and needs, and including consideration of the unique requirements of the not-for-profit community services sector, must be developed
- the current tax treatment of housing be reformed to shift benefits from wealthy home-owners to low-income renters and low-income earners seeking to buy their first property
 - capital gains should be taxed at the same rate as other income
 - negative gearing should be capped
 - the Commonwealth Rental Assistance Scheme should be indexed to increases in private rental rates
 - the First Home Owners Grant should be directed solely at low-income earners

3 | General comments on the role, design and objectives of the system

Q1.1: *In considering the community's aspirations for the type of society that Australia should become over the next two decades and beyond, which key features should inform or drive the future design of the Australian tax-transfer system?*

The Uniting Church in Australia believes that taxation should be regarded as the primary means for ensuring the equitable distribution of wealth and that the raising of public money through taxation is done to ensure that everyone in the community has access to the means to live a decent life. For this reason taxation policy and income support policy are both essential. Taxation is one of the most important tools at our disposal for achieving economic justice and is vital to a flourishing society. Taxation should be viewed as an obligation, and not a burden to be endured, to ensure that:

- Governments fulfil their responsibilities in provision of services ensuring that all people in the community have their basic needs met (a matter of human rights) and correcting the inequitable distribution of income and access to goods, services and resources which results when distribution is left to the private sector and market mechanisms;
- Governments deliver on their responsibility to protect the human rights of all Australians which includes their economic, political and social rights which requires horizontal and vertical redistribution of income which is only possible through taxation; and
- People contribute, according to their means, to the well-being of the whole community, through redistribution and the provision of goods and services.

We believe that the central design principle of the tax system must, therefore, be the capacity to raise enough revenue to meet the democratic demands for government expenditure.

The Uniting Church believes that the tax system should be structured to encourage sustainable and ethical economic activity, facilitate individual and community wellbeing and inclusion and discourage activities that exacerbate social and economic disadvantage and vulnerability. It is reasonable to demand government expenditure on service provision to the disadvantaged and vulnerable to ensure they have a decent life and can access the services they need to facilitate economic and social participation. It is also reasonable to expect that a nation as prosperous as Australia has an adequate income support system that enables all Australians to access the components of a decent life:

- financial security for a reasonable standard of living
- decent and meaningful work
- education
- access to adequate healthcare
- secure housing
- appropriate social services

- opportunities for cultural, technological, social and spiritual development
- the right to participate in decision-making in the community and
- lively, safe and inclusive communities.

In the Uniting Church's initial submission³ we stressed that the following principles should underpin reform of Australia's tax and transfer system and we reiterate them here:

1. Equity must be the first priority – across generations, across income groups and sources of income and across industries. This principle is discussed in greater detail in section 4 of this submission.

2. People matter – especially those who are disadvantaged and vulnerable

The tax and transfer system needs to provide support when people are most in need. The issue here is balancing this support with appropriate incentives to allow people to take up employment where and when they are able. This issue is discussed in greater detail in section 6.

3. Not-for-profit community sector services are essential to the economic and social life of Australia.

The tax treatment of the not-for-profit sector and its employees is discussed in the submission from UnitingCare Australia to this round of the review.

4. Tax rates need to be set at a level that ensures governments have the capacity to meet community expectations about services, income support and national infrastructure

The Australian community places a high value in the adequate provision of public services for all, particularly in health and education. The nation-wide deficiencies in these areas and in others such as infrastructure and public transport are well-noted.

By the standards of the developed world Australia is a low tax country. It is important to note that many of the European countries including France and Belgium have government revenue at more than 40 percent of GDP while in the case of Sweden it is over 50 percent of GDP, whereas in Australia that figure has been around 30 percent for the last decade. Our small revenue base makes it hard for the government to invest significantly in the kinds of services that not just help build economies, but help build societies. While the language of 'burden' can conceal it, the fact is that taxes have a number of significant benefits as a policy tool. Not only do they raise revenue to fund essential services, but they also serve, when designed well, to perform the important task of increasing social inclusion and community cohesion through deliberate income redistribution.

³ This submission is available at: http://www.unitingjustice.org.au/images/pdfs/issues/economic-justice/submissions/uca_henrytaxsubmission_311008.pdf

5. Simplicity and efficiency (balanced against equity) are important— for example, complicated exemptions should be removed and replaced with transparent allocation of government funds according to policy priorities. But where complexity is needed to ensure fairness, the system should give priority to fairness. The issue of simplicity is discussed in greater detail in section 7.
6. Reform of the tax system can contribute to reducing regulatory burden and increasing transparency of government support.

Q1.2: Assuming that the absolute size of government will not fall, should (and can) Australia nonetheless aim to reduce the burden of taxation over time by promoting faster economic growth than public spending growth? Can it be demonstrated that alternative tax policies could help deliver that outcome?

As stated earlier, we do not believe that the taxation burden in Australia is onerous and do not therefore desire to see it decreased even further.

We reject the use of the language of ‘burden’ and urge politicians and government bureaucrats to refrain from using such terms.

The contention that Australians would be better off if taxes were reduced is often taken as a statement of fact. In order to address this assertion we must compare the reality of social and economic outcomes in high taxed and low taxed countries. Findings from a study conducted by Brooks and Hwong published in 2006 show that high-tax countries (Sweden, Norway, Denmark and Finland were looked at in this study) have been more successful in achieving their social objectives than low-tax countries (the United Kingdom, the United States, Canada, Ireland, Australia and New Zealand), and have done so with no economic penalty.⁴

The language of burden is particularly inappropriate given that Australia is a relatively low taxing country by OECD standards, and in light of the current levels of poverty, exclusion and inadequate public services and infrastructure which persist in this country.

Public spending should always at least match growth in overall national revenue. However, we believe that the assumption that continual economic growth, be it fast or slow, must always be the goal of public policy is inherently flawed. Particularly in the light of the threat posed by human-induced climate change and the current global financial crisis, we believe that we must reconsider the emphasis we have placed on continual economic growth. It is now a matter of survival that we need to declare limits to ‘growth’ measured in such a way. An economic system that measures ‘progress’ in terms of continually increasing GDP, company profits, personal disposable income, and consumer spending and continually decreasing levels of taxation is inherently flawed.

Such a system does not reflect a regard for a holistic approach to human wellbeing but rather counts human wellbeing, at best, as a secondary and derivative goal measured

⁴ Brooks, N, and T. Hwong, ‘The Social Benefits and Economic Costs of Taxation: A Comparison of High- and Low-Tax Countries’, Canadian Centre for Policy Alternatives, December 2006, available: http://www.policyalternatives.ca/documents/National_Office_Pubs/2006/Benefits_and_Costs_of_Taxation.pdf

only in financial terms: if economic growth slows, halts or reverses, human wellbeing is threatened because the capacity of individuals to consume is threatened.

The current (global) economic system also fails to account for ecological wellbeing. Unrestrained consumerism, encouraged as a necessary plank for economic growth, is inflicting serious damage on the biosphere and the single-minded pursuit of corporations to deliver profit to their shareholders has resulted in the destruction of rivers and forests around the world and the devastation of Indigenous communities and cultures.

This model also measures people's value to society in terms of their productiveness, quantified in financial terms, and defines their individual success by how well they perform as consumers and measures it by the personal and conspicuous consumption of material goods. Education, for example, is now directed at producing 'productive' human beings rather than curious, effective and creative life-long learners engaged with the world around them. Consumerism is entrenched in our society and internalised within our self-understanding as it has come to be an answer to our deep and genuine needs for belonging, connection and security.

We believe that growth as it is measured by ever-increasing wealth and profits is actually not 'progress' in a sense that reflects the creative flourishing of human beings, but simply an expression of greed. It is time to reconsider this understanding of human progress if we are to ensure the planet for future generations. We must recognise and accommodate the inherently cyclical nature of economies. Above all we must re-imagine and redefine our success as societies and nations according to how well we support what is necessary for the flourishing of all people.

While the taxation system is just one aspect of our economic system, it is one of the most important tools for ensuring that all people in our society have what they need to flourish. It is of vital importance that it be based on principles which reflect an holistic and sustainable understanding of human progress.

4 | Equity

The Uniting Church believes that the taxation system is our primary means for ensuring the equitable distribution of wealth and the raising of public money, our “common wealth”, in order that we may ensure that basic needs of people in society are met. It is the community’s tool for ensuring an equitable society. This notion of equity encompasses several different elements.

The tax and transfer system needs to be progressive and produce vertical equity, that is to ensure that the burden of tax falls on those best able to pay.

Horizontal equity is based on the idea of recognising difference, requiring that people in the same position pay the same amount of tax, and people in different positions (both social and financial) pay different levels of tax. We believe that socially beneficial personal and family circumstances, such as the raising of children and caring for a disabled, sick or elderly relative, require additional support through the tax and transfer system. We do not, however, support difference that arises because of the type of income a person receives, such as more favourable treatment of investment income over earned income.

The principle of intergenerational equity in relation to the tax and transfer system will become increasingly important as the Australian population ages and a higher proportion of the community becomes dependent on a smaller number of people in the workforce. Although it is generally accepted that taxpayers should support non-taxpayers (those that are unable to work), this principle needs to be restricted to ensure the burden in the declining number of people of working age is not too great.

The ‘ability to pay’ principle should apply in relation to income received by all Australians, regardless of their age or the source of their income. A person’s age is not, of itself, indicative of their ability to pay taxes, which should rather be determined by measures of income and wealth as is the case for assessing eligibility for transfer payments.

5 | The revenue mix

Q3.1: What problems, if any, are generated by the overall mix of taxes in Australia on business and labour income, consumption, transactions and assets, and what changes, if any, should be made?

We refute the often-aided claim from business that Australia's corporate tax rate is high by international standards. We reject the notion that any increase in Australia's corporate tax rate will have a dramatic adverse effect on Australia's international competitiveness. In reality, a complex interplay of numerous factors, including tax rates but also including wage levels, industry regulations and political stability affect this competitiveness. Company tax falls mainly on local and overseas shareholders (of which the majority are high income earners) through the application of the dividend imputation system and to a lesser extent through cost and pricing structures on employees and consumers (who are more likely to be low or middle income earners).⁵ If company tax revenue was to fall as a result of a decreased tax rate, the shortfall in revenue would need to be balanced by increases in tax in other areas. It would be of concern if consumption taxes were increased as, in the absence of comprehensive safeguards and compensation mechanism, such taxes are highly socially regressive. Furthermore, the tax system is currently structured in such a way that any reduction in corporate tax rates would not generally benefit local investors as they would lose imputation credits, but would rather mainly benefit overseas investors.⁶

The Uniting Church does not advocate difference in the basis of taxation for different classes of income, such as income from labour compared to income from capital. In particular the concessional treatment of capital gains has resulted in significant distortions in the tax base and in investment decisions, as discussed in greater detail in section 7.

Q3.4: Assuming no increase in the rate or base of the GST, what principles should guide the future development of other consumption taxes in Australia, and is there a need to change the role and structure of such taxes?

Most consumption taxes aside from the GST are 'sin taxes', which are implemented where behaviour, if untaxed, would otherwise have a detrimental effect on society and/or the taxpayer. Where a consumption tax can be justified as addressing an externality, such as increased public health costs, the tax has an overall public benefit.

Currently, however revenue from such taxes is directed into the general taxation revenue pool, and is not automatically hypothecated to the specific social issue being addressed by the tax. This issue was raised in the recent public debate about the "alcopops" tax. Consumption taxes, such as those on alcohol, tobacco and gambling, must be structured so that revenue is allocated to programs and services aimed to reduce the prevalence of personally and socially-destructive behaviours.

⁵ ACOSS, 'Submission to the Taxation Review Panel – Strong foundations: Reforming the tax and social security systems', October 2008, p.15, available: http://acoss.org.au/upload/publications/submissions/5252__ACOSS%20Submission%20-%20Directions%20for%20tax.pdf

⁶ *ibid.*

It is also the case that consumption taxes often have the greatest incidence among those who can least afford the extra cost and who have less access to the kinds of social supports necessary to change personal behaviour, primarily low-income and marginalised communities. This requires not necessarily the abolition of such taxes but greater and more appropriate government support for the necessary preventative and rehabilitative health and social services needed in these communities.

Overall, the implementation of consumption taxes must be done very selectively as they, including the GST, have the potential to contribute to inflation and erode the value of transfer payments, affecting the progressivity of the tax and transfer system overall.

Q3.5: Could greater application of user charges, rather than general taxes, in the funding of government services or infrastructure bring social, environmental or economic benefits?

The application of user charges must be based on the principle that people should not be charged for public goods that are necessary for health, safety and an adequate standard of living. These goods and services should be provided freely for all through the provision of government taxation revenue. It is reasonable to expect that a nation as prosperous as Australia has a level of taxation that enables all Australians to access the components of a decent life and flourish as individuals – financial security for a reasonable standard of living, decent and meaningful work, education, access to adequate healthcare, secure housing, appropriate social services, opportunities for cultural, technological, social and spiritual development, the right to participate in decision-making in the community and lively, safe and inclusive communities.

Where user charges are applied to change behaviour and bring about economic, social or environmental benefits, appropriate alternatives must be in place to enable everyone to choose the lower cost or more environmentally-friendly (for example) option. For example if government is trying to influence the public to reduce their use of private vehicles and therefore applies a charge to motorways, adequate public transport alternatives must be available at a low cost for everyone. Where user charges are applied, adequate safety nets should be in place to ensure disadvantaged or low-income Australians are not unfairly denied access.

6 | Personal tax and transfers

Many of the various tax deductions, exemptions and concessions are in general only accessible to middle and high income taxpayers (in the areas of housing and superannuation in particular). This coupled with many deficiencies in the transfer payments made to low-income and disadvantaged individuals and families has created a tax and transfer system which is currently largely unequal, inefficient and unfair.

Tax assistance for families

In general, tax assistance for families is poorly targeted and unduly complex. The interplay between increased income and the withdrawal of benefits has created a substantial problem with very high Effective Marginal Tax Rates (EMTR), particularly for low and middle income households. This problem was highlighted in the initial Uniting Church submission to this review, as well as in submissions from many other welfare and community organisations. This must be addressed when addressing poverty and social exclusion, as workforce participation is acknowledged to be a key method for reducing poverty in families.

The particular outcome of high EMTRs is to discourage the second earner in a family from increasing participation in the workforce. Many people earning below-average wage rates face effective marginal tax rates higher than people earning three or four times as much. One in seven two parent families and one in five sole parent families faces an EMTR in excess of 50 percent as a consequence of the withdrawal of family tax benefits.⁷ This could be addressed by adopting the principle in the formation of tax and transfer policy that no person should face an EMTR higher than the top marginal rate. Numerous community organisations and forums⁸ have advocated a strengthened version of Family Tax Benefit A and a government-funded parental leave scheme to replace Family Tax Benefit B, the Dependent Spouse Rebate and the Baby Bonus, to both address the problems of high EMTRs for families and the complexity in the system. We would support such a change.

Newstart Allowance

There are also particular problems evident with the Newstart unemployment payment and the EMTRs for those receiving the payment. This issue is particularly pertinent in the current economic climate where more people are at risk of becoming unemployed. The Newstart payment has fallen significantly behind pension payments and this gap is a significant barrier for sole parents and people with disabilities who are eligible for pensions but decide to try a job which then does not work out. Such actions may lead to ineligibility for a pension payment or considerable delays in being restored to it. This

⁷ Harding, A. et al, 'AMP.NATSEM Income and Wealth Report 14 - Trends in Effective Marginal Tax Rates 1996-97 to 2006-07', September 2006, available: <http://www.amp.com.au/vgn-ext-templating/v/index.jsp?vgnextoid=e00350665a6cc110VgnVCM1000002930410aRCRD&srch=1>

⁸ This proposal was put forward by Prof. Julian Disney at the ACOSS Annual Conference on 3 April 2009. Proposals to replace the universal baby bonus with a well designed paid parental leave have also been put forward by the Brotherhood of St Laurence (in its paper 'The Case for Change: A Snapshot Analysis of the Australian Tax System') and the Australian Council of Trade Unions (in its submission to the Productivity Commission's Inquiry into Paid Maternity, Paternity and Parental Leave).

effect is compounded by the prospect of ineligibility for Pensioner Concession Cards or Health Care Cards.

The gap between different types of payments has arisen from the different indexation of various pensions and allowances, as the Newstart Allowance is indexed to CPI whereas pensions such as the Disability Support Pension and Parenting Payment Single are indexed to average weekly earnings (which have tended to increase faster than the CPI). We recommend that the Newstart Allowance be substantially increased and indexed in the same manner as pensions.

We also believe that the Newstart payment does not reflect the current workforce realities where the only feasible work opportunities for many people are casual, part-time or intermittent work. The current means-testing system for averaging income does not adequately recognise fluctuating patterns of employment and should therefore be improved to allow incomes to be averaged over a longer period.

Concessions for savings and superannuation

Incentives to save should be targeted at low-income earners, given that low-income people are more likely to be adversely affected by having to forego wages in order to increase savings and higher-income earners do not necessarily require added incentives to save.⁹

Superannuation concessions will cost the 2008-09 budget \$24.6 billion, comparable to the \$26.7 billion annual cost of the age pension and constituting one fifth of income tax revenue, and continued growth in costs of the concessions will continue contributing to the cost of Australia's ageing population.¹⁰ These concessions overwhelmingly benefit higher-income earners and currently provide almost no benefit to low-income taxpayers.

A more equitable approach to superannuation contributions would be to tax contributions in the same manner as other remuneration and then provide a credit or co-contribution. This would be more progressive than current concessions, such as matching contributions at a decreasing rate up to a modest level. Such a scheme could be accompanied by abolishing or replacing the pension income test in order to still provide an equitable system for retirement income, and one which is less complex and more cost-effective.

Q4.2: What is the appropriate distribution of income tax across income levels and how should it differ from the current distribution? Should governments seek to maintain a similar distribution over time, or should they fix the value of current tax thresholds through indexation?

The Australian tax system is based on the principle of progressivity. We do not believe, however, that the decline in the top marginal tax rate from over 60 percent in the late 1980s to 45 percent today, equating to a significant reduction in the tax burden faced by very high income earners, is representative of an adequately progressive tax system.

⁹ Disney, J., 'Taxation, Social Justice and Economic Development', address to the ACOSS National Conference, April 3 2009, available http://acoss.org.au/upload/publications/papers/5794__ACOSS%20Conference%20Papers%20Day2.pdf

¹⁰ Ingles, D., 'The great superannuation tax concession rot', The Australia Institute, Research Paper No. 61, Feb 2009

In addition, the increased thresholds, when compared to average weekly earnings, have reduced the progressivity of the system. We do not believe it appropriate that someone earning \$180 000 a year should be taxed at the same marginal tax rate as someone earning \$1 000 000.¹¹ An essential step therefore in restoring the principle of progressivity in the tax system would be to introduce a new top marginal tax rate for very high income earners. This would also raise significant revenue and ensure that the system is keeping pace with the acceleration in incomes being paid to the executives of large corporations. We note here that the UK Government has recently announced a 50 percent tax rate for high income earners.

This change is also crucial for ensuring that the amount of revenue needed to fund the necessary government services for all citizens is raised in an equitable manner. As a study published by the Centre for Economic Policy Research at ANU shows, the overall burden of the Australian tax system has shifted towards low and average-income families with two wage earners,¹² which we believe contradicts the principle of vertical equity.

¹¹ Denniss, R., 'The case for a new top tax rate', The Australia Institute, Research Paper No. 58, Oct 2008

¹² Apps, P. and R. Rees, 'Taxation, Labour Supply and Saving', Australian National University, Centre for Economic Policy Research, Discussion Paper No. 590, December 2008, available: <http://cepr.anu.edu.au/pdf/DP590.pdf>

7 | Complexity and simplicity

Q8.3: To what extent might policy objectives be traded off to achieve a simpler system? In what areas should efficiency, equity or choice be traded off for simplicity?

The pursuit of simplicity and efficiency in the tax system is important, but simplicity should not be seen as a goal in its own right. A simple tax system can be a very unfair system and lead to distortions. The UK poll tax is an example of this. Mechanisms designed to increase equity or take account of the idiosyncratic circumstances of some disadvantaged groups tend to reduce simplicity, such measures must be evaluated against a broader set of criteria than just simplicity. Embodying the principle of horizontal equity, for example, into the tax and transfer system will require some degree of complexity in eligibility requirements and different concessions and transfers. We should be prepared to allow inefficiencies in favour of fairness in such circumstances.

Tax expenditures

An unambiguous way to simplify the tax system, whilst increasing the amount of tax revenue available to fund essential services and improving the equity in the system, is to remove or tighten a wide range of tax exemptions. This is particularly pertinent in the current economic context, where the Federal budget will run into deficit and find it necessary to seek out opportunities to reduce gaps and loopholes in the tax system to legitimately increase tax revenue.

Such exemptions, also known as 'tax expenditures', impose significant costs on the Commonwealth Budget but are less transparent than direct expenditures incurred by the Commonwealth. That is, while each year the Government is required to seek parliamentary approval to appropriate funds for specific purposes, there is no such annual obligation to gain parliamentary approval for tax expenditures. That said, the Treasury does publish an annual summary of the nature and extent of tax expenditures, and this summary forms the basis of the following analysis. According to the Tax Expenditure Statement for the year 2008-09 the total cost of tax expenditures to the Commonwealth is projected to be \$52.5 billion, or 4.4 per cent of GDP compared to 3.7 per cent of GDP in 2003-04. Over the period 1984-85 to 2007-08, tax expenditures double as a proportion of public spending from 10.3 percent to 20.8 percent.¹³

Tax expenditures available to individuals tend to favour higher income earners as they are linked both to the income tax system and to private spending on social services. Most expenditures in Australia relate to the income tax system and because they are not capped, higher income earners receive greater benefit as they pay more tax.¹⁴ For example, the concessional treatment of capital gains is one of the most significant tax

¹³ Spies-Butcher, B and A. Stebbing, 'Reforming Australia's hidden welfare state: Tax expenditures as welfare for the rich', February 2009, p.6, available:

http://cpd.org.au/sites/cpd/files/CPD_OP6_Reforming_Australias_Hidden_Welfare_State_Spies-Butcher&Stebbing_0.pdf

¹⁴ *ibid.* p.7

expenditures, and 38.6 percent of tax of all capital gains income is attributable to the top 1 percent of income earners.¹⁵

We believe that there needs to be a clear policy justification for each tax expenditure, in accordance with community priorities and need.

For example, in the absence of increased direct government funding to community service organisations, Fringe Benefits Tax concessions provided to the sector are crucial for ensuring its financial viability and ability to attract skilled employees. This issue is canvassed comprehensively in the submission from UnitingCare Australia, an agency of the National Assembly of the Uniting Church representing the network of UnitingCare community service providers.

¹⁵ Ingles, D., 'Tax equity: Reforming capital gains taxation in Australia', The Australia Institute, Technical Brief No. 1, April 2009, available: <https://www.tai.org.au/>

8 | Housing

Q10.1: *What should be the objective of the tax-transfer system in respect of housing? Should there be assistance for housing over other assets or services? Should assistance be based on housing tenures? Should assistance be focused on people with low incomes? Should assistance differ between public and private tenants?*

Q10.2: *What role, if any, should the tax-transfer system play in respect of housing affordability?*

Q10.3: *Recognising the influence that some taxes and transfers have on the use of housing and residential land, what changes, if any, should be made to ensure the housing stock and residential land are use efficiently?*

Accessible, affordable and secure housing provides the foundation for the wellbeing and participation of all citizens in our community. All people in our community are entitled to an adequate standard of housing. The experience of 'housing stress', where the cost of adequate and appropriate housing leaves insufficient funds for food, clothing, transport and other necessities severely impairs the ability of individuals and families to thrive personally and participate in their communities.

As the determinant of net income, the tax and transfer system impacts significantly first on the funds available to households to cover housing costs and also on the cost and availability of rental accommodation and owner-occupied housing through concessions available in relation to investment in housing. As such the tax and transfer system must be structured to acknowledge the different marketplaces for renters, owner-occupiers and investors, and the interplay between them.

In general, the current tax treatment of housing favours wealthy home-owners and investors over low-income renters and low-income earners looking to buy their first property. The lack of affordable rental accommodation and increases in housing prices, particular in capital cities, have been well noted in politics and the media. The inflation of house prices and rents has forced many families to live in outer-urban areas often a long distance from workplaces. This impact has tended to be greatest for people who have lower incomes and less employment opportunities.

Capital gains tax

Whilst we acknowledge that Capital Gains Tax impacts on asset and investment decisions more generally, capital gains concessions impact significantly on the housing market. Capital gains concessions for investors are mainly enjoyed by higher income individuals, and also involve an important element of horizontal inequity (tax payers using other savings and investment options receive less favourable tax treatment). We believe that, for investors, capital gains should be taxed at the same marginal rates as other income, to discourage the concentration of housing investment to where the capital gain is the greatest.

Negative gearing

Increases in rents have also been fuelled by allowances for negative gearing. Interest and other landlord expenses should be deductible only against income from the same source (i.e. property investment and not from a salary), as is the case in the United States.¹⁶ There should also be a cap on negative gearing, so for example investors with numerous properties are not able to access it. This would complement the positive work already being done to address rental affordability for low-income households through the National Rental Affordability Scheme. It should be noted however, that as reported by the Senate Select Committee on Housing Affordability in Australia in 2008¹⁷, the total value of concessions and exemptions for capital gains tax, land tax and negative gearing far outweigh the funding allocated to address housing affordability and the housing needs of low income households through the Commonwealth-State Housing Agreement, National Rental Affordability Scheme and Housing Affordability Fund.

Commonwealth Rent Assistance Scheme

The main form of short-term assistance to low-income renters is the Commonwealth Rent Assistance Scheme. The CRA is indexed to CPI but increases in private rental rates have increased at rates above the CPI in recent years, adversely affecting many low-income recipients of the CRA. This has the effect of displacing low-income renters to outer-suburbs and non-metropolitan areas, many of which are not served adequately by public transport, schools, healthcare and other services.

We recommend that the Commonwealth Rent Assistance Scheme be indexed to increases in private rental rates rather than the general CPI figure, to maintain the affordability of private rental accommodation for low-income earners.

The First Home Owners Grant

The First Home Owners Grant has impact significantly on the cost of housing at the lower end of the housing market. The uncertainty over whether the grant will be continued has created a housing bubble as first home buyers rush into the market to take advantage of the grant. A tax system which reduces other pressures currently pushing up house prices (such as capital gains and negative gearing concessions) should negate the need for the First Home Owners Grant to be available to all first home buyers, and allow funding to instead be directed to a grant for only low-income earners and to addressing the broader housing needs of low-income and disadvantaged households.¹⁸

¹⁶ Disney, J., op. cit.

¹⁷ 'Report of the Senate Select Committee on Housing Affordability in Australia, Chapter 4 – Factors influencing the demand for housing', available: http://www.aph.gov.au/senate/committee/hsaf_ctte/report/c04.htm

¹⁸ The proposal to make the First Home Owners Grant available to low-income earners only and direct funds into addressing the broader housing needs of low income Australians was made by ACOSS in its submission to the Senate Select Committee on Housing Affordability in Australia.

9 | The environment

Q13.2: *Are there features of the tax-transfer system which encourage poor environmental outcomes and how might such outcomes be addressed?*

The fringe benefits arrangements for motor vehicles in the absence of any tax benefit for public transport users significantly favours the continued preference and unnecessary use of private vehicles for many people. Concessions should be available for genuine use of work cars, however they should have tight requirements for justification of the need for a work-related vehicle. In other cases the concessional rates of FBT application should be reviewed to reflect the true cost to society of operating such vehicles.

Public transport passes, such as Sydney's Travelpass system should be eligible for concessional FBT, and structured to encourage regular and ongoing use.

The increase in tax revenue created by a tightening of FBT concessions for motor vehicles should be allocated to increasing public investment in much-needed public transport in outer-urban areas.

10 | Conclusion

The Uniting Church in Australia believes that taxation is a profoundly moral matter and is one of the most important tools at our disposal for achieving economic justice and a flourishing society. Taxation is the primary means for ensuring governments have the capacity to fulfil their responsibilities in the provision of services to ensure that all people in the community have their basic needs met. We believe that Australia's small revenue base makes it very difficult for governments to fulfil this task, and recommend changes to top marginal tax rates and tax expenditures to address this.

Within the tax and transfer system equity must be the first priority – across generations, income groups, sources of income and industries. We believe that numerous features of the system currently work against the principle of equity and many of the various tax deductions, exemptions and concessions favour higher income earners (such as capital gains tax and superannuation arrangements for example). The Uniting Church does not advocate for difference in the basis of taxation for different classes of income and believes that all income should face the same marginal tax rates.

The transfer system must provide support when people are most in need and balance this support with appropriate incentives to allow people to take up employment where and when they are able. Currently, the interplay between increased income and the withdrawal of benefits has created a significant problem with very high Effective Marginal Tax Rates, particularly for low and middle income households. As such we recommend changes in the structure of tax assistance for families, the Newstart Allowance and pensions.

We commend the Henry Review on its work so far and appreciate the opportunity to respond to this very important review of the Australian tax and transfer system.