ASSOCIATION OF CONSULTING ENGINEERS AUSTRALIA

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AUSTRALIA'S FUTURE TAX SYSTEM

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ACEA SUBMISSION

ACEA response to the call for submissions on Australia's Future Tax and Transfer System

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The Association of Consulting Engineers Australia (ACEA) is an industry body representing the business interests of firms providing engineering, technology and management consultancy services.

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INTRODUCTION

The Association of Consulting Engineers Australia (ACEA) is an industry body representing the business interests of firms providing engineering, technology and management consultancy services.

There are over 260 firms, from large multidisciplinary corporations to small niche practices, across a range of engineering fields represented by ACEA with a total of some 45,000 employees.

ACEA presents a unified voice for the industry and supports the profession by upholding a professional code of ethics and enhancing the commercial environment in which firms operate through strong representation and influential lobbying activities. ACEA also supports members in all aspects of their business including risk management, contractual issues, professional indemnity insurance, occupational health and safety, procurement practices, workplace/industrial relations, client relations, marketing, education and business development.

EXECUTIVE SUMMARY

ACEA welcomes the opportunity to provide assistance in the design and implementation of Australia's Future Tax and Transfer System. ACEA agrees with the overriding premise of the present review. Australia needs a simple, equitable and efficient tax system that positions Australia to deal with the demographic, social, economic and environmental challenges of the 21st century, both domestically and internationally. ACEA believes much of Australia's future growth will come from how the tax system is designed today.

Presently, Australia is in the middle of one of its most expansive periods of growth and prosperity. Over 15 years of growth has changed expectations of the economy's capabilities. It has also highlighted that Australia's policy mix must continually focus on long term strategies and investments if Australia is able to realise its full potential.

The recent events in global financial markets provide an opportunity to conduct a stocktake to consider how Australia can strengthen its position and ensure its future prosperity.

A good tax system will not distort business and individual decision making. A poor tax system, by contrast though, will encourage business to consider tax issues ahead of other criteria for investment. Part of good tax design is to ensure that the tax system is kept as simple as possible. This means that the underlying purpose and principles behind the design of a tax can be clearly identified. It should be clear what is being taxed, who has to pay the tax and how the tax is calculated. Clear legislation with minimal hidden implications is needed to reduce both tax avoidance and the unproductive administrative burden for the Government, business and individuals. The tax system should always include a clear and unambiguous definition of the tax base and simple means of collection, this unfortunately is not the case in a number of incidences.

Australia's tax system must be efficient. A number of factors can cause the tax system to become inefficient and increase compliance costs. Reducing the complexity in calculating tax liabilities and improving the clarity in legislation is the key to reducing overall level of compliance costs. Australia's tax system must also be equitable. Taxes should raise the targeted amount of revenue for Government expenditure with minimal distortion on an individual's behaviour. The tax system must treat each taxpayer equally, whilst ensuring the Government's revenue stability.

Below ACEA has identified a number of areas that can make Australia's tax system simpler, more efficient and equitable. In addition this submission seeks to provide the appropriate balance between taxation of the returns from work, investment, consumption and proposes a number of initiatives to address climate change.

Finally, in a federation like Australia where taxes are imposed by a number of Governments, the roles and responsibilities of the Federal and State Governments also needs to be considered carefully. Improving the intergovernmental transfer system and improving the efficiency and reliability of the State tax base is at the front of this discussion.

In summary, ACEA hopes that any changes to the taxation system will simultaneously serve to address the challenges of today: to increase Australia's international competitiveness, to improve workforce participation, to retain skills including older workers, and to improve capital formation. With these measures combined, ACEA believes that the economy will be better prepared for the long term challenges that Australia faces.

ACEA recommendations for increasing global competitiveness

Recommendation 1: Reduce the Top Personal Tax Rate

The Government should seek to reduce the number of tax thresholds to preferably no more than two over an appropriate period of time.

Recommendation 2: Align the Top Personal Tax Rate with the Company Rate

The top personal tax rates should be gradually reduced to the same level as the corporate rate. While ambitious, this will also have positive equity effects between other aspects of the tax system and should be highlighted.

Recommendation 3: Eliminate Bracket Creep

Ensure the elimination of bracket creep via the annual indexation of taxation thresholds to inflation. This will ensure average tax rates are maintained for the Australia public.

Recommendation 4: Reduce the Corporate Tax Rate

Continue to reduce Australia's corporate tax rate to increase international competitiveness and promote entrepreneurship in Australia.

Recommendation 5: Tax incentives for Infrastructure

Reintroduce tax incentives for large infrastructure projects to make returns more attractive for large institutional investment funds.

Recommendation 6: Improve intergovernmental efficiency

Introduce intergovernmental transfers and stronger revenue raising capacity of the States, through improvements in the efficiency of the State tax systems. Particular emphasis should be given to infrastructure development. This should include simplifying the overly complicated system of horizontal fiscal equalisation (HFE) reducing the extent to which the States cross subsidise each other and quarantining Specific Purpose Payments (SPP).

ACEA recommendations for increasing workforce participation

Recommendation 7: Retention of older workers

The tax transfer system can play important role in the retention of older workers. This should be encouraged by the Australian Government through initiatives such as the Mature Age workers offset.

Recommendation 8: Parental leave

Introduce a national paid parental leave scheme which is fully funded by the Federal Government. A Federal Government paid maternity leave scheme should be funded for 14 weeks at the Federal Minimum wage which is currently $543.78 per week ($14.31 per hour).

Government payments should be made directly to the employee by the Government, not through the employer, and should be paid to the mother except in circumstances where she is not the primary care giver. Furthermore a national paid parental leave scheme should not impose financial or administrative obligations on employers.[1] For employers who wish to do so, they may top up the Federal Governments contribution to maintain an employee's wages.

Recommendation 9: No FBT on child care

All childcare services provided by an employer should be exempt from FBT. Where the employer does not provide child care (which is the case for many small businesses) the employee should be able to claim a child care deduction against their personal tax.

ACEA Recommendations for improving efficiency in the taxation system

Recommendation 10: Harmonise payroll tax

Australian States and Territories to harmonise inconsistent payroll legislation to improve administrative arrangements across all jurisdictions, with the aim of eventually removing payroll tax completely.

Recommendation 11: Removal of non-core imposition of FBT

Remove fringe benefits tax from items which are incurred as part of everyday business.

Recommendation 12: Introduce a Step Rate CGT

Introduce a stepped rate CGT to significantly reduce the burden of tax on capital gains and encourage investment in the Australian economy.

Recommendation 13: Carry back of losses to offset earlier gains

Introduce carry back of losses to offset earlier gains. This recommendation would improve loss utilization and improve incentives for taking on risk.

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[1] Inquiry into Paid Maternity Leave, Paternity and Parental Leave, NSW Business Chamber submission to Productivity Commission, 2008

Recommendation 14: CGT rollover provisions

Increase access to CGT rollover provisions as they are currently restrictive and onerous.

Recommendation 15: A more competitive Capital Gains Tax regime

Reduce the CGT rate to the company tax rate at 30 per cent this would encourage individuals to invest more in income bearing assets.

Recommendation 16: Taxing Super at two stages only

Super should be taxed at two points in the cycle only. This would provide a greater incentive to invest more in superannuation and lessen the burden on future Governments. It will also bring the system in line with international practice.

Recommendation 17: Increasing Employee Contributions

Compulsory superannuation contributions should firstly be sought from employees.

Recommendation 18: Government Co Contribution Scheme

Increase voluntary superannuation contributions through changes to the Governments Co-contribution scheme.

ACEA Recommendation to improve education and innovation

Recommendation 19: An Education and Training Tax Concession

Introduce an Education and Training Tax Concession, at the rate of 125 percent, for employers who spend more than 2 per cent of payroll on education and training activities per year.

ACEA recommendations for sustainability

Recommendation 20: Green Depreciation

To increase the adoption of energy efficient measures in the building industry Green Depreciation should be adopted for existing non-residential buildings that meet a specified environmental standard.

Recommendation 21: White Certificates

Introduce a national White Certificates scheme to promote energy efficient measure amongst business and households.

Recommendation 22: Funding for Retro Fitting

Financial assistance mechanisms such as grants, subsidies and rebates should be available for improvements in energy efficient measures undertaken by households and business.

Recommendation 23: Household Assistance Measures

Funds could be made available for small scale upgrades including insulation, or large scale energy enhancements like solar panels, with no means testing, providing improved transition rather than simply subsidising households.

INTERNATIONAL COMPETITIVENESS

Australia's consulting engineering industry employs over 124,000 people in an industry that competes globally for skilled workers. Personal income tax levels play an important role in encouraging the retention and attraction of skilled engineering professionals to Australia. The level of income tax is therefore a major contributor to attracting engineering professionals and providing internationally competitive services.

Currently the consulting engineering industry is experiencing shortages in both professional and paraprofessional engineering roles. ACEA predicts that these are likely to continue for a further five years at least given the proposed volume of infrastructure spending by all levels of government.

ACEA believes that in order to improve the international competiveness of the consulting engineering industry a structured tax reform is needed. This includes, reducing personal income tax rates, increasing income tax thresholds and, indexing tax thresholds.

At present Australia's high rates of personal income taxation:

- Inhibit Australia's international competitiveness;
- Are a barrier to higher workforce participation;
- Make it harder for consulting engineering companies to attract skills from overseas; and
- Reduce incentives to invest in human resources.

Reduce the number of income tax thresholds

ACEA proposes reducing the number of thresholds to no more than two. In addition ACEA proposes reducing the top personal tax rate, over a number of years, to bring it into line with the company tax rate of 30 per cent. At present the large gap between the top personal marginal income and the corporate tax rate may encourage tax structuring via the redefinition of personal income as company income.

The alignment of the top marginal tax rate with the company tax rate is recommended because:

- It removes a tax related incentive for dividends to be paid by companies, allowing for increased corporate savings and investment;
- It removes an incentive for wealthier tax payers to set up companies and trusts to decrease overall tax levels; and
- Taxpayers with a private company can rearrange their affairs to maximise the income earned by the company and maximise the deductions taken at the individual level.

Indexing tax thresholds to inflation to address bracket creep

ACEA proposes indexing tax thresholds to inflation. This will create an ideal opportunity for maintaining average tax rates of personal income taxation. Indexing to inflation would be sufficient to eliminate bracket creep, which operates to increase the average rate of taxation without any real increase in personal income. Indexing to inflation would also ensure personal taxation revenue levels do not increase as a proportion on GDP, thereby providing additional savings for capital formation activities.

Company Taxation

The last reduction in Australia's corporate tax rate was 2002, with the rate falling by 4 percent to 30 per cent. This reduction saw Australia corporate tax rate ranked 9th lowest in the OECD, equal to Demark, Iceland and the United Kingdom. Presently the OECD corporate tax rate average is 26.6 cent meaning Australia is now the 21st lowest in the OECD, equal with New Zealand and Spain.

As a result, Australia collects a relatively high proportion of company taxation revenue as percentage of GDP. Currently company taxation revenue accounts for 6 percent of GDP. This is the fourth highest in the OECD, and well above the OECD average of 3.7 per cent, although it is recognised that the imputation system, as well as the strong performance of the Australian corporate sector compared with other OECD countries in recent years, has an impact on this.

What is clear though is that the international competiveness of Australia's corporate tax has been slowly eroded over the last decade. Lowering the corporate tax rate would lead to higher returns on invested capital, as a larger proportion of after tax revenue can be saved and then invested again. This savings investment cycle is essential to Australia's economic success and international competitiveness.

Infrastructure

The shortfall of Australia's infrastructure has been well documented. Bottlenecks at the ports, congestion on roads, struggling public transport, inadequate rail systems and straining electricity networks have all undermined Australia's growth potential.

In 2005 Engineers Australia undertook an analysis of Australia's Infrastructure. They produced a Report Card ranking Australia's infrastructure from A+ to FF. The report included roads (C), rail (C-), electricity (C+), gas (C+), ports (C+), water (C) and airports (B). Overall the report card gave Australia's infrastructure a C+, which is by no means exceptional.

There is an immediate and economic need to attract more investment from the private sector. To achieve this, the Commonwealth Government should offer incentives through the tax system similar to previous efforts where the Federal Government has offered concessional tax treatment for infrastructure projects.

An example is the concessional tax treatment enjoyed for interest received from debt finance provided to certain infrastructure projects before 14 February 1997. This form of concession fell under the Australian Infrastructure Borrowing Offset Tax Scheme (IBOTS) which is no longer available. The Australian IBOTS allowed resident infrastructure financiers to obtain a tax rebate on interest received from infrastructure providers, while the providers forgo a tax deduction on that interest. By reducing the cost of borrowing, such essential projects can become more commercially viable.

Additionally, up to May 2004 the interest received from debt used to finance certain land transport projects was also concessionally taxed. This form of project financing helped to establish many necessary toll roads such as Westlink M7 and Western Sydney orbital.

ACEA recommends that a similar scheme could be reinvigorated in line with the Government's desire to augment the nation's capital works programme. However, ACEA would remind reformers that, when the scheme was active the cost was capped at $75m per year which made the scheme largely ineffective in developing infrastructure. Therefore the scheme should be reconsidered with the allocation of a more appropriate cap.

Federal State Relations

Key areas of Australia's public service provision are subject to complex arrangements of joint Government involvement which has lead to a number of inefficiencies that impinge on Australia's productivity. ACEA believes that defining the roles and responsibilities of Governments is important in key areas of service provisions such as infrastructure.

Blurred boundaries in decision making and funding arrangements have created some cost and blame shifting. Government's at every level need to be able to work together to overcome these challenges.

A more simple system of intergovernmental transfers and stronger revenue raising capacity of the States, together with improvements in the efficiency of the State tax systems, would improve the ability of State Governments to meet expenditure responsibilities. In addition improved financial outcomes would allow for State Governments to undertake meaningful taxation reform, while reducing the administrative burden and costs of taxpayers generally.

ACEA recommendations for increasing global competitiveness

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WORKFORCE PARTICIPATION

Workforce participation is another of the key challenges facing Australia as working families try to balance work and family life, while at the same time Australia has an unprecedented aging population.

Retention of older workers

The engineering profession has an aging demographic, as evidenced by the following Engineers Australia announcement in June 2008,

"During the five years to the 2011 Census, we estimate that 70,000 engineering professionals will have retired. At current rates, the expected 45,000 graduates will not even cover the losses over the same period. It is possible that current professional engineering skills shortages will double by 2011: the numbers are unnerving for Australia's future."

The skills and knowledge of older workers need to be retained within the consulting engineering industry to ensure its continued sustainability. This is particularly important as the Government plans to deliver a challenging array of infrastructure required to provide for Australia's growing mobility and trade needs.

ACEA proposes that changes to the Mature Age Workers Offset is one such scheme that should be considered. This initiative is aimed at encouraging older workers to remain working or rejoin the workforce. The offset is available to workers aged 55 years and over who have net income from working of less than $63,000. However, the maximum offset has been $500 since it became available on 1 July 2004.

Reforms to the mature age worker offset would greatly enhance the retention of a skilled and essential segment of the population and reduce the gap in the workforce created when older workers retire.

Paid Maternity Leave

The consulting engineering workplace is predominately populated by male workers. ACEA's 2008 Skills Survey Report (a stocktake survey looking at the impact of skills shortages in the ACEA membership) recorded that male employees represented over 60% of the workplace in both entry level and mid-level engineers (up to 10 years work experience), only 10% of females were represented at senior engineering level (10 plus years experience) and 5% at the Principal level.

ACEA endorses the proposed introduction of a national paid parental leave scheme which is fully funded by the Federal Government. The national paid maternity leave scheme should be designed in a way to provide support for the mother and child immediately after child birth, assist parents with a more appropriate work life balance, and increase the workforce participation rate. ACEA believes that this will have a major positive impact in attracting and retaining more females into consulting engineering.

FBT on Childcare

Another taxation policy that impacts unfairly upon employers is the provision of childcare facilities or payments. Currently child care is not subject to FBT when the employer provides the child care on its business premises. However, if the employer pays for child care provided on different premises, then it is subject to FBT.

ACEA acknowledges that employers have an important role to play in developing appropriate work and family policies. However, current rules in regard to FBT on child care discriminate between those firms that are physically able to provide child care on premises and those who cannot.

Many firms, typically small firms, are not able to provide onsite childcare services. The current FBT arrangements therefore discourage employers from offering childcare services. This decreases the possibility of early return to work and the individual's contribution to the economy.

ACEA proposes that the scope of the existing FBT exemption for onsite childcare be increased so that employers can provide childcare to an employee that is FBT free. Removing FBT on child care will allow employees and employers to come to mutual agreements on family friendly working arrangements which will result in increased workforce participation by allowing for more parents to return to work. Modelling by Econtech[2] suggests a full FBT exemption for child care would cost around $137 million per year.

Where the employer does not provide child care (which is the case for many small businesses) the employee should be able to claim a child care deduction against their personal tax.

ACEA recommendations for increasing workforce participation

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The tax transfer system can play important role in the retention of older workers. This should be encouraged by the Australian Government through initiatives such as the Mature Age workers offset.

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Introduce a national paid parental leave scheme which is fully funded by the Federal Government. A Federal Government paid maternity leave scheme should be funded for 14 weeks at the Federal Minimum wage which is currently $543.78 per week ($14.31 per hour).

Government payments should be made to the employee directly by the Government, not through the employer, and should be paid to the mother except in circumstances where she is not the primary care giver. Furthermore a national paid parental leave scheme should not impose financial or administrative obligations on employers.[3] For employers who wish to do so, they may top up the Federal Governments contribution to maintain an employee's wages.

Recommendation 9: No FBT on child care

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EFFICIENCY IN THE TAXATION SYSTEM

In preparing a response to the Government's Rethinking Regulation Report 2006, ACEA surveyed a sample of its members to identify the cost of business regulation compliance incurred by the consulting engineering industry. This sample examined small, medium and large consulting engineering firms and asked them to identify their estimated costs per annum in complying with unnecessarily burdensome, complex, redundant or duplicate regulation.

[2] Budget Impacts Of Changes In Child Care: Tax Benefits By Econtech Pty Ltd: 1 December 2006

[3] Inquiry into Paid Maternity Leave, Paternity and Parental Leave, NSW Business Chamber submission to Productivity Commission, 2008

The results showed the following:

- Sole traders and small firms' (firms with a staff of up to 50) incur on average $40,000 per year each in unnecessary compliance costs.
- Medium and large firms (firms with staff of 50 plus) incur on average$180,000 per year each in unnecessary compliance costs.
- Across the ACEA membership this represents an additional administrative burden totalling $18.5 million per annum caused by unnecessary regulation.

It is noted in the Treasury's paper Architecture of Australia's Tax and Transfer System (2008), that broader studies into compliance cost across Australia have been conducted and similar results found. The Treasury's paper refers to two major studies have been under taken to estimate the cost of compliance for taxpayers in Australia. The first study by the Australian School of Tax (ATAX) in 1997 that was commissioned by the Australian Tax Office (ATO) found that the compliance cost was equivalent to 7 percent of the tax revenue, while a second study by Jeff Pope in 1994 estimated that the cost was 11.9 percent of the tax revenue. The following table presents a summary of the findings from both studies.

Survey estimates of aggregate taxpayer compliance costs in Australia

	ATAX (a)		Pope	
	%GDP	% Tax revenue	%GDP	% Tax revenue
Personal Tax Payers	0.34	4	0.96 (b)	9.2 (b)
Business Tax Payers	1.02	9.4	1.14 (c)	6.6 (c)
All Tax Payers	1.36	7	2.1	11.9

(a) All Australian Government tax administrated by the ATO
(b) Personal Income
(c) Employers PAYE collections, FBT,Company Income tax , and wholesales tax
Source Evans et al (1997) , Pope (1994)

Given that in 2006-07 around $320 billion was collected in taxes from Commonwealth, State and local Governments[4], the total cost of compliance to Australian tax payers would range from between $22 billion and $38 billion based on ATAX and Pope calculations. A comparison with the State Governments' collection of around $48.9 billion per year[5] in own source tax revenue, $38 billion in compliance costs is a considerable amount.

It is understood that some costs associated with administration of the system are unavoidable. ACEA would however suggest that the figures above show that the extent of costs associated with compliance is overwhelming. In some cases the costs may even exceed the benefit in terms of revenue collected.

Businesses that suffer the most from excessive compliance costs are small businesses. These firms have fewer resources and lack the in depth understanding of Australia's tax system to navigate the myriad of taxes applicable to their business. This is again of considerable concern to the ACEA.

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[4] ABS 5506.0 - Taxation Revenue, Australia, 2006-07

[5] ABS 5506.0 - Taxation Revenue, Australia, 2006-07

The Consulting engineering industry comprises of some 16,600 businesses with roughly 660 businesses employing more than 20 people[6]. This leaves some 15,940 small businesses exhausting a considerable amount of time and money into complying with Australia's tax system.

Whilst this discussion has looked at compliance costs generally, there a number of areas of specific concern to the ACEA, including payroll tax, fringe benefits tax and capital gains tax.

Payroll tax

The inconsistent manner in which Australia's payroll tax is administered across Australian States and Territories result in complexities and inefficiencies for businesses of all sizes. ACEA strongly believes that the costs associated with complying with differing payroll tax schemes for employers who operate across multiple jurisdictions is overly time consuming, costly and in need of urgent reform.

The first objective for payroll tax reform would be the standardisation of inconsistent legislation across States and Territories. This would reduce costs associated with complying with differing legislation for firms who operate across multiple jurisdictions.

In particular, the States and Territories need to continue to work together to produce uniform payroll tax legislation and identical definitions of the payroll tax base. For example there currently exist differences in definitions of salaries, wages, employees, contractors and deemed employees. Ideally, State and Territory Governments should work together to achieve this objective. While the tax rates and thresholds may continue to be different, all of the definitional provisions and administrative provisions need to be the same.

Once harmonisation is achieved, State and Territory Governments need to set realistic time frames for completely removing payroll tax as it is imposed upon those who are endeavouring to undertake economic activity and provide employment.

Fringe Benefits Tax

The present fringe benefit tax system is overly complex and unpopular with employers as it creates excessive compliance costs for businesses and it has eliminated the benefits that arise in tax avoidance prevention.

Fringe benefits tax (FBT) is collected from employers, levied on a comprehensive base, imposed on the grossed-up value of fringe benefits, and taxed at a flat rate equal to the top personal income marginal tax rate.

Although a number of changes have been made to this tax since it was introduced in 1986 the complexities, economic inefficiencies and inequities of the tax have yet to be addressed. This is despite continued calls from a range of stakeholders calling for its reform.

For example, the Institute of Chartered Accountants Australia published a report in 2006[7], which made the case for reform. The Report states,

"*Today, fiscal surpluses characterise the Commonwealth Budget so Budget cost is far less important. Also, the raft of tax reforms introduced over recent years have now become widely accepted and understood. On the issue of employers being better placed to administer the taxation of fringe benefits than employees, the international evidence does not support this view, as the norm is for fringe benefits to be taxed as income in the hands of employees.*

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[6] 2008 Outlook for Consulting Engineering

[7] The Institute of Chartered Accountants 2006 Fringe Benefit Tax Design: Decision Time

In relation to compliance costs, there is no evidence that the Australian approach is fundamentally superior and, if anything, the evidence is that our uncompromising approach to taxing fringe benefits in the hands of employers has resulted in a system with some of the highest compliance costs."

The Institute of Chartered Accountants argues that three major reforms are required:

1. The taxation of fringe benefits in the hands of the employee (rather than the employer);
2. Valuing all benefits at cost (rather than some concessionally, such as with motor vehicles);
3. Raising the threshold below which minor fringe benefits are tax-exempt income.

ACEA agrees with the Institute that the current FBT system has gone beyond its original purpose of reducing tax avoidance and is in need of urgent reform.

It is also producing some unintended consequences, for example, the statutory formula encourages the wasteful use of cars. The FBT rules increase the concessionary benefit of having an employer-provided car the more kilometers that are driven. Employees have no incentive other than to maximise the number of kilometers they travel to reduce their FBT bills, thus contributing to greenhouse emissions.

It is ACEA's proposal that there should be removal of non-core imposition of FBT, meaning that fringe benefits tax should be removed from items which are incurred as part of everyday business.

Capital Gains Tax

The level of saving and investment in Australia influences not only job creation, productivity and innovation but also the level of economic growth. Lowering taxes on capital gains will encourage people to save and invest more as their after tax returns from investment are higher.

Australia's Capital Gains Tax (CGT) regime is largely uncompetitive by international standards. If Australia is to increase savings and investments then the cost of capital needs to be reduced. Higher rates of taxation on capital result in lower savings, investment and capital formation. A stepped rate CGT however effectively reduces the CGT burden based on the number of years the asset is held. By steadily reducing the amount of capital gains included in assessable income investors are rewarded for investing long term. The net capital gains would still then be taxed at the taxpayer's marginal tax rate.

ACEA supports the Australian Chamber of Commerce and Industry's (ACCI) 2004 taxation blueprint that proposed a stepped rate schedule regime that is reproduced below.

Possible Stepped Rate Schedule: ACCI

Less than 1 Year	100%
1-2 Years	50% (25% for Small Businesses with underlying active assets)
2-5 Years	25%
5-10 Years	10%
More than 10 Years	0% (i.e. tax free)

This ACCI proposal will reduce the complexities associated with record keeping. Furthermore, ACEA believes that the CGT paid on assets sold in years 1, 2 and 3 under the new schedule should be no higher than under the existing schedule.

Another issue often raised in regard to CGT is the lack of ability to carry back losses to offset earlier gains. Realised capital losses can presently be offset against any capital gains in the current tax year in order to obtain tax relief. However, this presents a timing constraint on realising the "tax benefit" of the capital loss.

Carry back of losses are currently employed by the United States (US), United Kingdom (UK), Canada, Ireland and the Netherlands. This form of policy will improve loss utilization and improve incentive for taking on risk. International practice would suggest that generally three years is considered to be long enough for this purpose. The greater the length of time in which losses can be offset against past gains, the larger the cost to Government.

CGT rollover provisions allow assets to be transferred between related entities without triggering a CGT event or other tax consequence. They also allow for the deferral of CGT on gains under special provisions of the law such as those applying for small business or from involuntary disposal of assets.

Recognising that CGT can act as an impediment to the efficient restructuring of business, the Government introduced a number of reforms to the rollover provisions to cope with acquisitions, takeovers and mergers. However, ACEA believes that the current rollover requirements are restrictive and onerous, making access to provisions very difficult.

The taxation of nominal capital gains increases the effective rate of taxation on real capital gains. If inflation is running at 3 per cent, then an asset that increases by 2 per cent will be subject to taxation despite the assets price falling in real terms. ACEA believes indexation is a necessary feature of capital gains taxation.

The current system taxes real capital gains at marginal rates, which acts as a disincentive to savings and investment by businesses and individuals. To encourage investment the CGT rate should be reduced to the company tax rate at 30 per cent. Introducing a capped 30 per cent tax rate on capital gains would provide a definite incentive for individuals to invest more in income bearing assets.

Superannuation

The intergenerational Report published by the Commonwealth Government in May 2002 outlined how demographic changes will affect Australia in years to come. The proportion of people relying on superannuation and Government pensions will nearly double over the next forty years. In response, Governments are considering a range of options some of which will affect employers considerably. Changes will affect a firm's profitability, their ability to grow and directly impact in many cases on Australia's international competitiveness.

To accommodate the additional stress on the superannuation system, a number of policy changes are available, including changing the level of taxation on superannuation contributions, where the tax occurs, increasing employee contributions or employer contributions and other initiatives to retain older workers.

Increases to the superannuation guarantee scheme by employers have been proposed. Potential changes included raising the compulsory employer contribution from 9 per cent to as high as 12 percent. However, ACEA believes that this would pose a considerable additional burden on employers at time where measures that lead to inflationary pressures need to be guarded.

On the other hand, introducing compulsory employee contributions have been proposed as a means to fund the ageing population. ACEA also believes that any increases in the superannuation guarantee should be made through the introduction of employee contributions. However it is unlikely that the incidence of tax will fall directly upon the employee. A loss in after-tax income would likely bring about a round of employee wage bargaining to restore after tax income. Therefore, the introduction of employee contribution would only further increase demands on already over burdened employers, which during a period of full-employment would be borne by the employer and be inflationary.

Introducing increased compulsory superannuation contribution by employees would be unpopular no matter the rate because it reduces after tax incomes of individuals i.e. another tax, all be it for future consumption by the individual. Importantly though it turns savings into funds available for investment and provides for future consumption.

Compulsory employee contributions could also have the effect of driving up wages as employees bargain with employers to restore their after tax incomes. This potentially could have the same effect as increasing compulsory employer contributions, especially for businesses experiencing skill shortages.

Furthermore, to ensure the Government superannuation scheme provides sufficient funding to accommodate Australia's changing demographic, superannuation needs to be an attractive investment for encouraging people to save more for retirement. The level of taxation can play a strong incentive to promote investing after-tax dollars into the scheme.

In the current climate, ACEA believes that policies designed to encourage the retention of elderly workers should be considered as an alternate to raising employer or employee contributions. Government incentives could retain older workers and offer incentives for older workers to rejoin the workforce. This could potentially postpone the reliance of individuals on superannuation payments. Presently the Government has in place the Mature Age Workers Offset Scheme – see discussed earlier.

A further option for reform is to improve the concessional tax treatment of the current superannuation scheme. Favourable tax treatment when compared to other forms of investment will encourage greater investment and lessen the burden on future generations. Australia is unique in the sense that it levies taxes on superannuation at three places. For example, New Zealand only taxes funds upon withdrawal, so tax is only incurred upon exit. ACEA believes that the Government should consider removing one tax on superannuation contributions either upon entry, earnings or exit. An equivalent level of taxation should then be introduced at the point of benefit only.

Other incentives to promote investing more after tax dollars into superannuation should be considered in the design of Australia's future tax system. The Government's co-contribution scheme is a viable option already supported by Governments to increase investment in super by low and middle income earners. Changes to the Government's Co-contribution scheme would support further investment by households and couples. Changes should include increasing allowances and changing various limits and exclusion to broaden the scheme for older more affluent workers closer to retirement.

ACEA Recommendations for improving efficiency in the taxation system

Recommendation 10: Harmonise payroll tax

Australian States and Territories to harmonise inconsistent payroll legislation to improve administrative arrangements across all jurisdictions, with the aim of eventually removing payroll tax completely.

Recommendation 11: Removal of non-core imposition of FBT

Remove fringe benefits tax from items which are incurred as part of everyday business.

Recommendation 12: Introduce a Step Rate CGT

Introduce a stepped rate CGT to significantly reduce the burden of tax on capital gains and encourage investment in the Australian economy.

Recommendation 13: Carry back of losses to offset earlier gains

Introduce carry back of losses to offset earlier gains. This recommendation would improve loss utilization and improve incentives for taking on risk.

Recommendation 14: CGT rollover provisions

Increase access to CGT rollover provisions as they are currently restrictive and onerous.

Recommendation 15: A more competitive Capital Gains Tax regime

Reduce the CGT rate to the company tax rate at 30 per cent this would encourage individuals to invest more in income bearing assets.

Recommendation 16: Taxing Super at two stages only

Super should be taxed at two points only in the cycle only. This would provide a greater incentive to invest more in superannuation and lessen the burden on future Governments. It will bring the system in line with international practice.

Recommendation 17: Increasing Employee Contributions

Compulsory superannuation contributions should firstly be sought from employees.

Recommendation 18: Government Co Contribution Scheme

Increase voluntary superannuation contributions through changes to the Governments Co-contribution scheme.

EDUCATION AND INNOVATION

The public sector used to play a major role in education and training of professions in the workplace. An example of this is engineers working within public works departments who would join as graduates and develop their skills working on a range of government owned projects. This traditional training ground for young engineers has gradually reduced because over the last twenty years public works departments have outsourced engineering design and project management to the private sector.

The private sector must now fulfil the function formally undertaken by Government. Business, particularly small business, can find it difficult to fund high levels of training. This problem has increased as the workforce has become more mobile. Generation Y employees wish to be more flexible and mobile in terms of their career and do not stay with the same employer for long periods. This is an issue for employers that invest significant sums in their training only to find that the employee leaves shortly thereafter. This means that the business does not see a return from that investment.

ACEA believes that is a need for the Commonwealth Government to support the education and training conducted by business. This is essential to continued economic growth through productivity gains and to facilitate the move to a more knowledge and service based economy.

The Government should provide extra support for companies that fund skills development opportunities for employees. Australia's tax system can play a fundamental role in achieving this outcome. The tax system has the potential to encourage individuals and employers to undertake higher levels of education and training.

Australian employers increasingly understand the importance of investing in the skills and knowledge of their employees. But without Government support, employers may tend to under invest in this area. Often the full benefit of training is not captured by one employer as the employee moves between places of employment relativity freely. This full benefit is then captured by the Australian economy as a whole.

Government incentives could then been seen as an investment by Government in the Australian workforce. The dividend form this investment will be higher incomes and higher company profits, increasing Government revenue, improving living standards and boosting economic growth.

The Government should examine a number of possibilities in this area. Providing an education and training tax concession for employers who spend more than 2 per cent of their payroll to formal, accredited, skills development courses is one such option.

Education and Training Tax Concession

ACEA's proposes an Education and Training Tax Concession to strengthen incentives for employers to invest in the skills and productivity of their employees as a highly skilled and adaptable workforce is essential to Australia's economic future.

An Education and Training Tax Concession would provide a tax concession for business when expenditure on education and training activities exceeds 2 per cent of payroll, per year. The concession would compensate business at a rate of 125 per cent of every dollar that exceeded the 2 percent threshold. Such an Education and Training Tax Concession would provide direct financial benefits to employers who invest in developing the skills of their employees. This type of scheme would be based upon each companies' desire to invest in their staffs' development. The scheme would also be optional, meaning it will not subject all firms to a compulsory training levy which has been previously proposed.

In order to claim the concession the eligibility criteria must be broad reaching, but simple for businesses to administer. The concession could be capped to manage the potential financial risk to the federal Government. Employers should only be able to claim the concession for applicable courses including but not limited to register training organisation and other courses that meet prudential guidelines.

The concession would drive innovation and productivity at the workplace by drawing more effectively on the talent and creativity of employees already in the firm. It would also increase the level of support available for existing workers to update and upgrade skills that support productivity, innovation and knowledge within the Australian economy.

ACEA Recommendation to improve education and innovation

Recommendation 19: An Education and Training Tax Concession

Introduce an Education and Training Tax Concession, at the rate of 125 percent, for employers who spend more than 2 per cent of payroll on education and training activities per year.

SUSTAINABILITY

The introduction of an Australian emissions trading scheme, now known as the Carbon Pollution Reduction Scheme (CPRS) has been identified as central to achieving the Government's goal of reducing Australia's greenhouse gas emissions by the year 2050.

The building sector is responsible for a large proportion of Australia's Green House Gas (GHG) emissions. The Australian Sustainable Built Environment Council's (ASBEC) Climate Change Task Group (CCTG) has identified complementary measures to the carbon pollution reduction scheme as an essential element in unlocking the GHG Abatement potential in the Building Sector.

Studies by the Centre for International Economics (CIE) commissioned by ASBEC CCTG for The Second Plank report[8] have shown that residential and non-residential buildings consume around 19 per cent of Australia's total energy use.[9]

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[8] ASBEC CCTG (2008) The Second Plank – Building a Low Carbon Economy with Energy Efficient Buildings

Energy use in the building sector is also rapidly increasing. The Centre for International Economics (CIE) estimates that the building industry is responsible for 23 per cent of Australia's total GHG emissions. Therefore, if measures are not introduced to reduce GHG emissions the residential sector emissions will increase by 78 per cent, while emissions by commercial buildings will more than double to 154 per cent by 2050.

In order to meet the Federal Government's GHG reduction targets the building sector can and should play a leading role in achieving GHG reductions. There are clear opportunities to reduce the levels of GHG in the short term. Significant gains are available now in the building sector without the need to invent and apply new technologies. CIE estimates that electricity demands in residential and commercial buildings can be halved by 2030, and reduced by more than 70 per cent by 2050 through energy efficiency measures. Furthermore, by 2050 Gross Domestic Product (GDP) could be improved by around $38 billion or 2 per cent per year if energy efficiency measures are adopted by the building sector.

Upgrading the energy efficiency of Australia's building assets will deliver a sustainable outcome. The rewards for investing in the energy efficiency potential of the building sector will flow through the entire economy.

The tax system needs to play an important role in encouraging the adoption of appropriate energy efficient measures. Australia's future tax system should not simply redistribute revenues generated by the carbon trading scheme to low and middle income earners. ACEA believes that, in the short term, transfers will be required to assist in the adjustment phase of the scheme, however this is not a sustainable long term policy. This means that to reduce the overall levels of GHG emissions incentives are needed to shift individuals and businesses away from heavy GHG emitting products to more energy efficient items.

Further, Government incentives will be required to change consumer behaviour. Incentives must be provided to reduce the costs associated with the transition to more energy efficient measures.

ACEA supports the following initiatives that have been proposed by the ASBEC CCTG to combat the growing emissions by the building sector.

Green Depreciation

ACEA supports a tax incentive for building owners to refurbish buildings to be more energy efficient, also known as Green Depreciation. Green Depreciation is a form of accelerated depreciation for buildings that meet a specified environmental standard. This would apply to existing non-residential buildings. The aim is to provide a strong incentive for building owners to refurbish their existing building stock. This would bring about a rapid reduction in the environmental footprint of the building sector.

The Australian Government would effectively finance the scheme through the tax expenditures. The proposed green depreciation scheme is projected to result in reduced revenue for the Australian Government of $568 million[10] over four years (a period spanned by the next budget year and three budgets out).

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[9]Centre for International Economics Capitalising on the Building Sectors to Lessen the Potential to Lessen the Cost of a Broad Based Emission Cut

[10] Green Depreciation: A preliminary Analysis, The Centre for International Economics October 2007

The foregone tax revenue is used by owners and operators of existing buildings to purchase savings in greenhouse gas (GHG) emissions. Some green buildings may use up to 70 per cent less energy than normal buildings. Given Australia's relatively high GHG emissions intensity factor for electricity generation, reducing the demand for electricity will reduce GHG emissions.

It is estimated[11] that the proposed Green depreciation arrangements could lead to the abatement of 203 Mt CO2 emissions over the medium term (eleven years). This is equivalent to removing 6.4 million cars from the road each year from 2007-08 to 2017-18.

White Certificates

A national White Certificate scheme would be very timely. Several states are in the process of implementing variants of a White Certificate scheme. A national scheme that applies to the residential and commercial building sector will minimise differences and enable a market on a larger, more efficient scale.

The scheme can be applied in many ways, but an approach already tested in Australia (in NSW) works by applying energy efficiency targets to the electricity retailers. The retailers are given flexibility in achieving this target by either implementing their own efficiency arrangements or purchasing efficiency certificates based on the performance of electricity customers in raising efficiency beyond a benchmark.

These arrangements make energy efficiency an asset that is able to be traded like a commodity and provide the building sector with an incentive to invest in additional energy efficiency. The scheme would provide a signal that would help overcome problems with bounded rationality and would place a price on externalities (where electricity savings and GHG savings are associated).

The scheme could be expanded to include a voluntary market allowing households and businesses to participate and be rewarded for energy efficiency.

Publically funded retro fits for residential and commercial buildings

Public funding of energy efficiency retrofits would require a range of Government funded financial assistance mechanisms for improvements undertaken by households and the commercial sector, i.e. grants, subsidies and rebates. Funding should be made available for and limited to investment opportunities with a proven ability to reduce energy consumption.

Public funding of building retrofit reduces the investment cost for energy consumers, therefore reducing the costs associated with transition and providing an additional incentive to undertake investment in energy efficiency. Public funding would ideally be sourced by the capital raised through the sale of permits from the CPRS.

ACEA believes that a significant portion of the capital should be allocated to households and building owners to incentivise them to invest in improving their energy efficiency. This contrasts with the broad views expressed in the CPRS Green Paper. The Paper suggests that assistance in the form of compensation may be the most appropriate means of helping household and business transition to a low carbon future.

While ACEA agrees that a limited amount of compensation may be appropriate in some instances (e.g. low income earners and pensioners) the majority of funds should be made available to a wide range of stakeholders in the form of incentives. These types of activities are more likely to change behaviour and move Australia toward reaching its goal of reducing carbon emissions now and into the future in a sustainable and socially accepted way.

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[11] Green Depreciation: A preliminary Analysis, The Centre for International Economics October 2007

Household Assistance Measures

The Green Paper outlines that all revenue from the sale of permits will be provided to households and business to ease the transition to a carbon constrained future.

Expanding the range of energy efficiency policies has the ability to address market barriers and failures that remain even after the introduction of the scheme. There are a range of measures available in this area to incentivize households and business.

When considering assistance for households the same principle of incentives versus handouts must exist to facilitate changes in behaviour. Households and small businesses can be assisted in the transition to a low carbon economy, particularly in helping low income households reduce their energy costs by making funds available and conditional for retro-fit improvements to homes that aid in energy being used more efficiently.

ACEA does not believe that means testing will result in the GHG emission reduction targets that the Australian Government would like achieved. This is because it does not incentivise behavioural change across all the Australian demographic. The faster a market is created for renewable energy sources the sooner the need for assistance will reduce. Household consumers of energy are looking for providers to delivery renewable and clean sources of energy. The only way to stimulate change is by a capital investment into renewable energy, which will create demand across all households in Australia.

The energy infrastructure in Australia is ageing therefore it should be possible to reduce some householder's reliance on the national grid. For example, those households that can afford to invest in new technologies like solar power could not only reduce their reliance on the national grid but could actually contribute to it where they are over-producing energy.

Also, funds could be made available for small scale upgrades like insulation, or large scale energy enhancements like solar panels, with no means testing. The premise should remain that all households will face challenges in adjusting to higher energy and goods prices and all households wanting to access funds for energy efficiency improvements should have access to these funds.

ACEA contends that the split of funds between business, households and energy intensive trade exposed industries should be reviewed periodically and based on incentives rather than hand-outs. Compensation does not have the benefit of allowing for significant behaviour change and will do little to limit GHG emissions.

Other policy measures

A policy option for encouraging energy efficiency in the building sector is to provide rates and charges relief (e.g. Stamp Duty) to encourage retrofit and investment in energy efficient buildings. This approach can be applied across the building sector including both investment property and owner-occupied buildings.

Another available option exists in the form of energy retailers financing energy efficiency improvements. This measure would aim to overcome the hurdle of the difference in timing of private costs and payback associated with energy efficiency investments (i.e. up-front expenditure and medium term cost recovery through lower electricity bills). Electricity retailers could finance the upfront cost of investment in energy efficiency and recoup the cost by retaining the resulting savings.

When considering policy options and initiatives to encourage energy efficiency measures and investment/research in renewable energy sources, education and awareness campaigns are important to any new approach being introduced. Campaigns to educate the business community as well as the wider population should occur in a range of ways, from awareness raising events to skills development and capacity building activities and materials.

Further Information on the initiatives highlighted above have been attached with the paper published by the Australian Council Built Environment Council (ASBEC) entitled "The second plank – Building a low carbon economy with energy efficient buildings".

ACEA recommendations for sustainability

Recommendation 20: Green Depreciation

To increase the adoption of energy efficient measures in the building industry Green Depreciation should be adopted for existing non-residential buildings that meet a specified environmental standard.

Recommendation 21: White Certificates

Introduce a national White Certificates scheme to promote energy efficient measure amongst business and households.

Recommendation 22: Funding for Retro Fitting

Financial assistance mechanisms such as grants, subsidies and rebates should be available for improvements in energy efficient measures undertaken by households and business.

Recommendation 23: Household Assistance Measures

Funds could be made available for small scale upgrades including insulation, or large scale energy enhancements like solar panels, with no means testing, providing improved transition rather than simply subsidising households.

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