MARITIME UNION OF AUSTRALIA (MUA)

SUBMISSION TO THE TAX REVIEW

AUSTRALIA'S FUTURE TAX SYSTEM

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1. Introduction

1.1 The Maritime Union of Australia (MUA) represents over 11,000 workers in the shipping (domestic and international), stevedoring, port services, offshore hydrocarbons, recreational dive tourism and inshore/offshore diving sectors of the Australian maritime industry.

1.2 Members of the MUA work in a range of occupations across all facets of the maritime sector including stevedoring and ports, on coastal cargo vessels (dry bulk cargo, liquid bulk cargo, refrigerated cargo, project cargo, container cargo, general cargo) as well as passenger vessels, towage vessels, salvage vessels, dredges, ferries, cruise ships and recreational dive tourism vessels. In the offshore oil and gas industry, MUA members work in a variety of occupations in vessels which support offshore oil and gas exploration e.g. on drilling rigs, seismic vessels; in offshore oil and gas construction projects including construction barges, pipe-layers, cable-layers, rock-dumpers, dredges, accommodation vessels, support vessels; and during offshore oil and gas production, on Floating Production Storage and Offtake Tankers (FPSOs), FSOs and support vessels. MUA members work on international bulk cargo vessels, petroleum product vessels and LNG tankers engaged in international LNG transportation.

2. A coinciding of the Tax Review and the Report of the Parliamentary Inquiry into Australia's shipping policy and regulation

2.1 The Union wishes to draw to the attention of the Tax Review the importance of taxation policy change that will be required to underpin future investment in the Australian shipping industry and to ensure that the Australian shipping industry, both its domestic and international dimensions, improve their competitiveness in this global industry.

2.2 The Report of the House of Representatives Standing Committee on Infrastructure, Transport, Regional Development and Local Government Inquiry into Australian coastal shipping policy and regulation is being released we understand late today, 20 October 2008, and given that submissions to the Tax Review closed on 17 October 2008 (we were provided with a one day extension till cob today 20 October 2008) we regret that we cannot provide a detailed submission to you based on the Parliamentary Inquiry's Report Findings and Recommendations.

2.3 Nevertheless, we are hopeful that the Parliamentary Inquiry Report will address both corporate taxation issues associated with the shipping industry and seafarer income taxation issues. In addition we are hopeful that the Report will address some tax anomalies that are undermining competitiveness in the Australian domestic shipping industry.

2.4 The MUA would request that we be provided with an opportunity to make a follow up submission to the Tax Review once the Parliamentary Inquiry Report is tabled and we have had an opportunity to address the tax implications of its Findings and Recommendations.

2.5 It is important that the Tax Review be aware that 23 of the 61 submissions to the Parliamentary Inquiry proposed changes to taxation arrangements for Australian shipping. Included among those submission are some of Australia's largest exporters, manufacturing and shipping companies, including CSR, BP, Visy, CSL and Rio Tinto. In addition, the Australian Shipowners Association (ASA) representing the majority of Australian shipowners, operators and crew supply companies proposed taxation reforms.

2.6 The Tax Review should also be aware that the Department of Infrastructure, Transport, Regional Development and Local Government has commissioned Meyrick and Associates to undertake modelling of the impact on GDP and tax revenues from changes in tax policy applying to the Australian shipping industry. We understand that the Meyrick and Associates work is to be provided to the Government in November 2008.

3. What are the key taxation issues for the Australian maritime industry?

Taxation measures to improve the international competitiveness of Australian shipping

3.1 There are two major and related taxation measures being proposed to improve the competitiveness of Australian international shipping – the introduction of a tonnage tax to replace the current corporate tax arrangements and changes to seafarers' income tax.

A tonnage tax – globally accepted as essential to a competitive shipping industry – now global best practice

3.2 All the nations that, over the past 10 years, have made the considered decision to grow their shipping industries have adopted a tonnage tax as a key policy instrument to achieve success. These nations include: Belgium, Cyprus, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Korea, Malta, Netherlands, Norway, Poland, Spain and the UK.

3.3 As an island nation, Australia is vitally dependent on an efficient and competitive shipping industry for the importation of most of our consumer goods, for the inputs for our vital agricultural sector and industrial equipment to support our key resources sector.

3.4 In addition, shipping is the key part of the supply chain for delivery of our commodity exports, where we are playing a vital role in provision of inputs necessary to underpin Asian manufacturing eg coal and iron ore, and energy for industry and households.

3.5 Australia is essential to Asian energy and food security and to power its manufacturing boom. And shipping is central to that logistics process.

Globally, the shipping industry is in a healthy state. Some nations have dramatically grown their share of the expanding shipping industry, with major benefits to their economies. But the beneficiaries of the booming shipping industry are unevenly spread across the globe. Furthermore, some nations are being penalised by the marginalisation of their investment in shipping. The MUA believes that Australia is one of those nations.

3.6 The fact is that Australia as a nation has not leveraged any real value out of its dependence on shipping, yet we have the 5th largest shipping task in the world as measured in tonne kilometers. Approximately 99% of Australia's merchandise trade is moved by sea, and over the next 12 years to 2020, containerised trade is forecast almost triple and non-containerised trade is expected to double.

3.7 An evaluation of those nations' that have made a conscious policy decision to leverage national interest benefits from shipping shows that in the main they have adopted a tonnage tax, usually in close parallel with other supportive policy measures. Most of the largest European countries have now implemented a tonnage tax. Japan has also recently done so and South Africa is considering a tonnage tax. All the evidence shows that a tonnage tax is the central policy instrument responsible for arresting the decline of shipping industries across Europe and for the expansion of European shipping. An overview of the various European tonnage tax models can be found in a 2007 Price Waterhouse Coopers publication entitled "*Choosing a profitable course: European tonnage tax regimes for the shipping industry*" available from www.pwc.com/transport.

3.8 A 2007 Report prepared for the UK Chamber of Shipping by Oxford Economics entitled "*The economic contribution of the UK shipping industry*", available from http://www.british-shipping.org/search/?site_search=oxford+economics&x=10&y=14 shows that since the introduction of the tonnage tax in the UK in 2000 the UK owned trading fleet has grown from a low of 617 ships to over 700 and the deadweight tonnage has risen from 7.2 M tons to nearly 18.0 M tons in 2007. Similarly, the number of ships on the UK register has grown from 379 to 629 since 2000.

3.9 The Oxford Economics report also quantifies the employment impact, the direct contribution to GDP and the contribution to government revenues. Rather than being a net drain on GDP, the UK experience shows that shipping is a major net contributor to GDP.

3.10 There are several designs for a tonnage tax used by different countries, but the basic concept remains the same across all the nations that have adopted it. It is important to recognise that the tonnage tax, to be successful and in determining eligibility, requires conditionality. Some of the conditions revolve around "Australianality" of the eligible tax entity eg its commercial and strategic management must reside in Australia. In addition, various training and employment objectives can be tied to beneficiaries, all aimed at maximising the overall gains for Australia in terms of contribution to GDP, contribution to tax revenues, development of a strategic industry etc.

3.11 The MUA submits to the Tax Review that in conjunction with the work being undertaken by the Department of Infrastructure, Transport, Regional Development and Local Government and having regard to the Findings and Recommendations of the Parliamentary Inquiry into shipping that the Tax Review establish a mechanism for shipping industry tax issues to be fully explored in conjunction with industry stakeholders and considered in the Consultation Paper being developed by the Tax Review.

Seafarer income tax – in need of urgent reform

3.12 In addition to training seafarers for both the international seafarer market and the domestic seafarer market, policy reform is required to ensure that Australian seafarers, highly regarded in the international market, can compete effectively in the international trade. The key policy initiative required to achieve this outcome is at a minimum, reform of Section 23G of the Income Tax Assessment Act.

3.13 In September 1994, a PAYE rebate scheme for ships trading internationally was adopted by Government as part of the resolution of a dispute over the sale of ANL. It commenced in July 1995. This was based on a scheme used in a number of shipping countries and was judged the most suitable of the schemes offered to the shipping industries of Japan, France, the UK, the USA, Norway, Denmark and Germany all of which were studied at the time.

3.14 The Independent Review of Australian Shipping (IRAS), undertaken by former Transport Ministers the Hon Peter Morris and the Hon John Sharp for the Australian Shipowners Association, found that the existing requirement for Australian resident taxpayers who are seafarers to pay domestic rates of tax on income earned overseas (i.e. working in international shipping) makes them uncompetitive against seafarers from other developed economies. For example, a British seafarer working a minimum of 181 days a year on vessels engaged in international voyages pays no personal income tax, meaning the employer can engage such employees for the actual salary cost.

3.15 Other OECD nations such as France, Germany, Netherlands, Denmark, Norway as well as Asian nations such as Singapore and Korea have similar concessionary income tax arrangements for their seafarers.

3.16 While Australian law (S23G of the *Income Tax Assessment Act 1936* (ITAA) provides for concessionary tax treatment for residents working overseas, a technical ruling that seafaring employment on the high seas does not constitute work overseas has ruled Australian seafarers ineligible for such tax concessions, thus increasing their employment cost and rendering them less competitive in international shipping.

3.17 The Senate Employment, Workplace Relations and Education Committee, in its report on its inquiry into workforce challenges in the transport industry in 2007 recommended that S23G of the ITAA be reviewed. It said:

"The committee recommends that section 23AG of the Income Tax Assessment Act 1936 be reviewed, and the meaning of 'foreign service' for income tax purposes be clarified so that Australian seafarers are not

disadvantaged in their earnings capacity relative to seafarers of other nations when working on foreign-flagged vessels on the high seas."

3.18 It is our submission that such a reform has independent merit, but importantly, is a critical complement to the proposal for a tonnage tax. Such a reform is an important complementary measure for employers who opt into the tonnage tax regime because:

- They have made a commitment to establish their strategic and commercial management in the developed economy; and
- They have made a commitment to train and employ nationals:

and therefore require supportive measures to ensure that competitiveness is enhanced.

3.19 As a result we propose that should a tonnage tax be considered in Australia, that any employer who opts into a tonnage tax regime be entitled to a rebate of 100% of the tax that would have been withheld from the seafarers income and paid to the ATO in relation to each seafarer that is employed on a tonnage tax ship that operates in the international shipping trade for 80% or more of its cargo in any financial year.

Favourable depreciation measures – common to shipping industries

3.20 Favourable depreciation are a common feature of the fiscal settings for the shipping industries of various shipping nations. Depreciation measures include:

- accelerated depreciation, which has a shorter depreciation period;
- advanced depreciation where depreciation is allowed before the actual acquisition of vessels;
- initial depreciation with an additional depreciation ratio over normal depreciation in the year of vessel acquisition; and
- favourable depreciation rates for vessel acquisition.

3.21 The measure of accelerated depreciation is most commonly applied in the global shipping industry. We submit to the Tax review that it consider this measure for Australian shipping, subject to the Findings and Recommendations of the Inquiry into shipping.

3.22 Attitudes of fiscal authorities in different countries with regard to the accounting life of a ship vary considerably, with normal depreciation periods ranging between five and 25 years. It is worth noting, however, that the shipping industry is characterised by the rapid technical progress and the correspondingly early economic obsolescence of assets – the ships. This makes accelerated depreciation an important means of fiscal relief for shipping investment.

3.23 In Australia, the 1984 Crawford Financial package provided for depreciation of 20% per annum commencing in the year prior to commissioning (previously 6.25% p.a.), provided that the ships achieved manning levels determined by a manning committee. In May 1996, the Coalition Government announced legislation to terminate the provisions on accelerated depreciation.

3.24 In the US, under the accelerated depreciation system for shipping investment, by using the liberalised provisions for computing depreciation a business can recapture 50% more of its investments in a fixed asset during the first half of the asset's useful life than it can when limited to a straight line depreciation as in actual depreciation.

3.25 Accelerated depreciation does not increase the total tax free allowances for capital consumption.

The tax treatment of bunker fuel - inequitable

3.26 The MUA wishes to draw to the attention of the Tax Review an apparent inequity in the pricing of bunker fuel used for bunkering arising from a differing tax regime applying to Australian registered ships on the one hand, and foreign registered ships on the other, insofar as those ships operate in the Australian coasting trade. Bunker is defined as the fuel that powers the engine of a ship and bunkering is the term used to define 're-fuelling' of a ship.

3.27 Item 5 subsection 38-185(1) of GST Act provides that export of goods that are to be consumed on international flights or voyages will be GST-free. Item 5 provides that a supply is GST-free if it is a supply of:

(a) aircraft's stores, or spare parts, for use, consumption or sale on an aircraft on a flight that has a destination outside Australia; or

(b) ship's stores, or spare parts, for use, consumption or sale on a ship on a voyage that has a destination outside Australia;

whether or not part of the flight or voyage involves a journey between places in Australia.

3.28 Thus, where a ship bunkers in Australia, and is on a voyage that has a destination outside Australia, the bunker fuel for the ship will be considered as `ships stores' and thus GST-free. It would not matter whether or not part of the flight or voyage involves a journey between places within Australia.

3.29 The effect of this tax regime is that foreign registered ships that are granted a Single Voyage Permit pursuant to section 286 of the *Navigation Act 1912*, which are in effect competing with Australian registered ships in the coasting trade, have a tax advantage over Australian registered ships. This is not only contrary to the principle of competitive neutrality which is being strongly promoted in decisions on reforming Australia's transport and logistics sector emanating from the Council of Australian Governments (COAG) but it favours foreign shipping in the Australian coasting trade.

3.30 Some of the foreign vessels that are attracting this tax advantage are in fact Flags of Convenience (FOC) ships. We submit to the Tax Inquiry that it is anomalous that Australian taxation policy favours foreign shipping over Australian shipping. Worse however, that such a policy is actually encouraging FOC ships, which are a potential safety and security risk, into the Australian coasting trade at a time when Australia is investing heavily in securing its borders through a robust maritime security regime, and when

there is a Parliamentary Inquiry Report that we are sure will promote an expansion of a competitive Australian shipping industry.

Customs duty on bunker fuel – inequitable

3.31 MUA advice received from the Australian Customs Service indicates that there is a distinction in customs duty payable on bunker or shipping fuels between ships engaged on coastal voyages as opposed to international voyages. Ships engaged in international voyages do not pay customs duty on bunker, meaning their bunker is up to 30% cheaper than the price paid for bunker by ship owners and ship operators licenced under the *Navigation Act 1912* to operate in the Australian coasting trade.

3.32 The effect of this discrepancy, and therefore price differential, is that it provides unfair competition for Australian ship owners and ship operators engaged in the coasting trade where the Government issues a Single Voyage Permit (SVP) pursuant to section 286 of the *Navigation Act 1912*. A ship to which an SVP is issued is a ship on an international voyage which just happens to be plying between two or more Australian ports as part of that international voyage and is permitted to carry coastal cargo between those Australian ports.

3.33 The customs duty advantage would also apply to vessels issued with a Continuing Voyage Permit (CVP) on those voyages involving a coastal voyage where an international voyage is also part of the overall voyage eg the 3 monthly voyages required to ensure compliance with the CVP condition requiring the vessel to leave Australia at least once every 3 months.

3.34 Vessels issued with SVPs (and CVPs under certain circumstances) are not required to pay customs duty on the fuel used or purchased to carry coastal cargo, unlike the requirement on an Australian licenced vessel which is competing with that foreign vessel for the coastal cargo.

3.35 This outcome is not only contrary to the principle of competitive neutrality which is being strongly promoted in decisions on reforming Australia's transport and logistics sector emanating from the Council of Australian Governments (COAG) but it favours foreign shipping in the Australian coasting trade to the direct detriment of domestic ship owners and ship operators.

3.36 Agfain, we submit to the Tax Review that it is anomalous that Australian customs duty policy favours foreign shipping over Australian shipping.