

To: AFTS Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

Submission on Australia's Future Tax System

A. Tax Incentives For Environmental Outcomes

A reformed tax system should provide a robust framework of taxation incentives or rewards for sustained environmental performance at the individual household / taxpayer level.

Example:

Take current state stamp duty on property transfers (generally a state tax issue):

- If a property were exempt from the stamp duty requirement, the owner could expect to gain the amount of the stamp duty in negotiating the sale price with a prospective purchaser – effectively an increase in market value;
- People will do a lot to protect or enhance the value of their property, and there is often a conflict between environmental values and capital improvements – the incentive approach would level this out considerably;
- Property purchasers with environmental attitudes and convictions are expected to willingly pay more for an accredited property – provided the stamp duty waiver can be secured into the future by appropriate choices, decisions and behaviours.

The current system of stamp duty collection is an enormous asset in state finance terms but is increasingly becoming a liability in public policy terms. Converting it into a principal driver of environmental sustainability would achieve an enormous amount of social good will, and create an enduring legacy.

The proposed regime requires substantial development in terms of the details, including levels of qualification, methods of validation, means of administration and so forth. However, working closely on the backbone of current developments in property transactions and information tracking is likely to make these issues relatively tractable.

Rationale

A system designed to include the environmental / sustainability component of property characteristics in the mainstream arena of market value would do a great deal to:

1. Encourage adoption of environmentally preferable methods, arrangements, materials, designs etc; and
2. Reduce the considerable cost of current approaches to engage the community through moral suasion, education and awareness raising.

Further, the internalisation of environmental considerations and characteristics in property values and choices would do much to reduce the currently wasteful costs of:

- Complex regulation and compliance issues associated with buildings, property, lifestyle and the environment;
- Ad-hoc policy debate and development and the resulting market uncertainties about the value of pursuing environmentally preferable objectives;
- Inefficient, one-off initiative funding and vacillating engagement programs that attempt to influence the market by moral suasion and other similar concepts.

The budget impact would be very gradual, due to different rates of uptake, but the energy and focus it would generate are expected to be vastly superior to other approaches employed to date.

B. Transparency in rates and charges associated with public services

A reformed tax system should address the plethora of current fees and charges that have been developed as indirect methods of funding certain public services.

Example:

In Victoria, as in some other states (I understand), domestic fire insurance charges include a compulsory contribution towards the public budget for fire brigade services.

- Many people (especially in the insurance sector) see this as distortionary and non-transparent.
- Those responsible for policy in the provision of fire brigade services are insulated from the financial realities of possible changes in policy or direction or quality of service;
- The community is confused about who is actually paying for what components and who is free-riding etc.

The current convoluted funding mechanisms and cash flows militates against sound policy development on a cost-benefit basis. The ever-shifting

boundaries between user-pays, council services and state services are almost impossible to understand.

These artifices stifle innovation and progress, and leave society with the impression that the Gordian knot of policy, fees and charges is truly unfathomable.

C. Public Accounting Rules Related to Developer Contributions

The new system must ensure that developer contributions (collected by local government and infrastructure authorities) be strictly accounted for as unearned income for tax and dividend purposes.

Example:

Developer contributions paid (and the value of assets contributed) to water authorities in Victoria are brought to book as cash income, with little or no offset in relation to operating cost. The result is that the contributions show up on the profit side of the accounts, and two thirds of the profit is paid to the state government under public authorities dividend provisions.

In turn, the authority has to pay for the assets out of retained earnings, which it can only raise by increasing revenue.

This practice has been much criticized by those who understand the implications, and has been defended by some on the basis that it is all evened out by depreciation.

My simple cash flow analysis indicates that the community ends up paying three dollars for every dollar spent on assets under this provision.

- This whole arrangement is distortionary and does not serve the public interest;
- It is so deeply ingrained into practice that even senior treasury officials are apparently unaware of its impacts on pricing;
- It is all the more ludicrous when considered alongside the onerous and exacting requirements for attributing and calculating payments (see for example, the reports prepared by the New South Wales Independent Pricing and Regulatory Tribunal). I suggest that the ultimate fate of the money is of far more importance than possible fine-tuning of the economic / costing models used to compute the amounts involved.
- The current situation is further distorted by the fact that developer charges paid to councils are not subject to PAD, whereas those paid to other government agencies are.

D. Ecosystem Services Payments

The new tax framework must lay the foundations for a system of paying landowners commercial rates for the provision of numerous environmental benefits (or ecosystem services).

Example:

Farmer Jones plans his mixed farming operation on the basis that, each year, he will earn sums of A, B, and C for his wheat, lucern and wool outputs, and will earn C and D for the value he provides in terms of intact box-ironbark woodland and streamside vegetation. Further, he knows that if he and his neighbours cooperate in reducing agricultural impacts on the local waterway, all their payments will increase by a percentage related to the improvement in downstream water quality.

Further, the ecosystem services payments are more secure sources of income, as prices only change slowly in response to assessed scarcity.

The value of this approach is that massive and allegedly inequitable allocations of finance to exceptional circumstances and other forms of rural assistance could be replaced by a mechanism that actually generates solid value to society.

- Society could assess all the environmental benefits it expects from land managers and pay them to produce those benefits;
- A possible education / collaboration /assurance mechanism is potentially viable through the residual landcare networks that exist in most states.
- A possible purchase mechanism is through the regional catchment or natural resources boards that have been established in most states but have little current influence on broad acre land management practices.
- Savings in expenditure on currently wasteful initiatives, programs, and on-off ventures could be converted into sustained benefit production.
- The environmental aspects of land management would be placed on an equal financial footing with other activities of production.

Detailed analysis of global progress with various form of regulation / encouragement of better agricultural practices has been undertaken by the OECD. The findings come down unequivocally on the side of abject failure. Clear market failure has been followed by regulatory failure (despite the laudable exceptions produced by deeply committed individuals).

Creation of a transparent market arrangement for these outcomes is unavoidable if we are going to save the bush, keep people on farms and avoid wasting money in the process. We owe it to future generations.

E. Commendation

My submission is brief but sincere, and is motivated by a personal drive for greater transparency and simplicity in an increasingly complex world, and the looming threat that our notions of inter-generational equity are fast evaporating in a warming climate..

I have more detailed thoughts, ideas and cost-benefit frameworks for most of the above, but do not have the time to document them here.

I commend the above to the AFTS secretariat for consideration.

Yours sincerely

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