



AUSTRALIAN INDUSTRY
GROUP

Comments on
The Independent Pricing and Regulatory Tribunal's
Review of State Taxation
Draft Report to the Treasurer

July 2008

Ai Group

The Australian Industry Group (Ai Group) is Australia's leading industry organisation representing 10,000 employers in manufacturing, construction, automotive, telecommunications, IT & call centres, transport, labour hire and other industries. Ai Group's members operate businesses of all sizes throughout Australia and represent a broad and expanding range of sectors. We provide comprehensive advice and assistance to help members run their businesses more effectively and to become more competitive on a domestic and international level.

Ai Group member companies operate businesses across New South Wales, Victoria and Queensland and we maintain strong partnerships with the Engineering Employers Association South Australia (EEASA) and the Chamber of Commerce and Industry in Western Australia (CCIWA).

Ai Group commends the Independent Pricing and Regulatory Tribunal on its very comprehensive and balanced Draft Report as part of its Review of State Taxation. We also appreciate the opportunity to provide comments ahead of your finalising the Report to the Treasurer.

In summary, Ai Group supports the short-term directions indicated in the report and also supports broadening the scope of reform of NSW's taxes through a thorough reassessment of intergovernmental financial relations. We support the underlying approach to improving the pattern of taxation in NSW. In general, we agree with both the broad directions suggested by the Report and the individual recommendations it makes. On the question of tax expenditures, we support the more transparent reporting and assessment of these while doubting the value of the particular recommendations made.

Further comments are made in relation to specific recommendations (retaining the numbering, though not necessarily the order of the Draft Report).

Interactions between State Taxes and the Commonwealth Grants Commission Methodologies

Recommendation 4. NSW Treasury should review in detail, before implementing the reforms recommended by this review, the interactions between the recommendations and the GST/Commonwealth Grants Commission grant allocation to NSW. Where the outcome is detrimental to good State tax reforms, this issue should be referred to COAG as an impediment to State reform designed to improve national competitiveness.

Recommendation 5. NSW Treasury should develop a capacity to better manage the interaction between the State's tax and expenditure policies and the Commonwealth Grant Commissions Horizontal Fiscal Equalisation (HFE) methodology. This will involve a regular report to the NSW Government on the impact the HFE methodology has on State (and national) tax (and expenditure) reform, for tabling at the Treasurer's Conference and referral to COAG. All tax proposals should include an assessment of the impact on the allocation of Commonwealth grants.

Ai Group has for some time called for the development of more coherent intergovernmental financial relations across the Australian federation. A fundamental motivation for our position is to widen the scope for taxation reform at the State/Territory level.

Ai Group supports the proposal for the NSW Treasury to investigate any impediments to State tax reform arising from approaches to grant allocation and to report its findings to COAG. We also suggest that any findings be referred to the Commonwealth Governments Review of the Future Tax System. We also support the NSW Treasury build its capacity to better manage the interactions between the States taxation and expenditure.

Recommendations for Reforming NSW Tax System Independently of Other States and the Commonwealth

Payroll tax

Recommendation 1. In the short term:

- *the tax free threshold for payroll tax should be reduced from \$600,000 pa to \$500,000 pa*
- *the payroll tax rate should be reduced from 6.0 per cent to 5.75 per cent.*

Recommendation 2. Over a two-year period, the payroll tax exemption for local councils should be removed and a corresponding increase in municipal rate-pegging limits should be phased in.

Recommendation 3. In the long term, the rate of payroll tax should be further reduced, with the long-term goal of achieving interstate parity in this rate.

While the recent State Budget has committed to lowering the payroll tax rate and raising and indexing the tax free threshold, Ai Group supports the direction of the reform advocated in Recommendation 1 of reducing the tax-free threshold relative to the new levels and lowering the payroll tax rate further.

While not a priority for Ai Group, we recognise that Recommendation 2 would improve the structure of the State's payroll tax system.

Ai Group strongly supports Recommendation 3.

Insurance taxes

Recommendation 6. In the short term, the stamp duty exemption for third party motor vehicle personal injury insurance should be abolished and that the standard rate of stamp duty for general insurance (Type A) be reduced from 9 per cent to 6 per cent.

Recommendation 7. In the short term, the statutory contributions by insurance companies to fund fire services should be replaced by a corresponding increase in the contributions by local councils, with a phased implementation and accommodating increases in the municipal rate cap.

Ai Group supports Recommendations 6 and 7.

Property taxes

Recommendation 8. In the short-term, the purchaser transfer duty should be reduced by replacing the existing first three rating levels with a single level for dutiable properties up to \$80,000 and reducing the duty payable up to this level to 1 per cent, with the details as shown in Tables 5.3 and 5.4.

Recommendation 9. In the short-term, the purchaser transfer duty rate scale should be indexed annually, based on an index of movements in all NSW property values.

Recommendation 10. In the medium term, consideration should be given to changing the tax unit for land tax from joint ownership to the individual, funded by a decrease in the tax-free threshold.

Recommendation 11. In the long term, the Government should develop a strategy for increasing property holding taxes (for example, broadening the land tax base, increasing the land tax rate and/or increasing municipal rates on land values) to fund substantial reductions in purchaser transfer duty and insurance taxes on a revenue-neutral basis. The strategy will need to consider carefully the impacts on the various taxpayers as well as the overall benefits to the community.

Ai Group supports Recommendations 8, 9 and 10.

In relation to Recommendation 11, Ai Group supports further examination of the proposal to reduce purchaser transfer duty and insurance taxes. We consider the proposed means of financing these (increasing property holding taxes) as worthy of examination. We note however there is likely to be considerable variation in overall efficiency and equity implications depending on the way property holding taxes were increased. We would be wary for example of a proposal to raise rates on the existing (narrow) land tax base. We anticipate that a closer examination would see greatest benefits from Recommendation 11 if initial priority was given to broadening the land tax base.

Taxes on the purchase and registration of motor vehicles

Recommendation 12. In the medium term, motor vehicle registration duty should be replaced with a revenue-neutral annual motor vehicle charge.

Recommendation 13. In the short term, stamp duty on purchases of caravans and camper trailers should be abolished.

Ai Group supports Recommendations 12 and 13.

Motor vehicle weight tax

Recommendation 14. In the medium term, after relevant transport policy issues have been resolved, consideration should be given to rationalising existing vehicle usage charges, including the motor vehicle weight tax, with well designed road use and congestion charges.

Ai Group supports a close consideration of Recommendation 14.

Possible new taxes

Recommendation 15. In the medium term, consideration should be given to increased use of environmental levies in the NSW tax system.

Ai Group supports a close consideration of Recommendation 15 as part of a strategy to significantly reduce the compliance burden of environmental regulation by replacing this form of regulation with more market-based approaches.

Tax expenditures

Recommendation 16. In the short term:

- *all tax expenditures should be brought on budget with an explicit appropriation shown and funded from the allocation for the relevant policy agency*
- *a ‘sunset clause’ should be specified for review of all tax expenditures, so that they lapse automatically unless Parliament agrees specifically to their renewal.*

Ai Group supports more transparent treatment of tax expenditures (which can be negative or positive) and agrees that there would be substantial benefits in clearer identification of tax expenditures. However, given that the definition of tax expenditures is inherently difficult and often controversial, we are very wary of Recommendation 16.

Tax expenditures compare the revenue that would have been collected under a benchmark tax system with that collected under the actual tax system. Both the specification of the benchmark tax system and the assumptions about differences in behaviour under the benchmark and actual tax systems are critical in identifying and measuring tax expenditures. In the absence of a definitive benchmark and given the considerable uncertainty about the behavioural impacts of taxation, we would anticipate limited value in the directions suggested in Recommendation 16.

User charges

Recommendation 17. In the short-term:

- *NSW user fees and charges practices should be benchmarked with those in other States*
- *guidelines and principles for these fees and charges should be developed*
- *all NSW user fees and charges not currently subject to a periodic review or indexation arrangement should be indexed annually to movements in the CPI.*

Ai Group supports Recommendation 17 and suggests that the indexation of user fees and charges not subject to periodic review should only occur after they have been openly benchmarked with those in other States and after they have been demonstrated to comply with the guidelines and principles proposed in Recommendation 17. the development of these guidelines and principles should be transparent and subject to consultation.

Tax administration

Recommendation 18. In the short term, priority should be given to the following strategies to further strengthen the efficiency and effectiveness of tax administration in NSW:

- *ongoing investment in the renewal and development of IT systems*
- *further improvements in data management and in data sharing with other NSW government agencies*
- *greater functional specialisation in some areas to address issues of high value or critical importance to revenue collection*
- *increased use of formal performance evaluation techniques such as performance benchmarking and tax gap studies.*

Ai Group supports Recommendation 18.

Reforming the NSW Tax System through Cooperative Federalism

Recommendation 19. NSW should advocate that a joint Commonwealth-State review be undertaken of the options for further expanding efficient Commonwealth taxes to fund the reduction or abolition of inefficient State taxes.

Recommendation 20. The States and the Commonwealth should give further consideration to tax reassignment to the States, and/or revenue sharing to encourage and promote State tax reform.

Recommendation 21. NSW should seek a direction from the Treasurers' Conference to the Commonwealth Grants Commission that HFE procedures be amended to quarantine fiscal transfers that are compensating adjustments for State tax reform.

Recommendation 22. NSW should seek amendments to the Horizontal Fiscal Equalisation (HFE) methodology for national tax reforms or changes in grant sharing arrangements to ensure individual States have incentives to introduce tax reforms that are in the State and national interest. This could include quarantining some taxes in part or in full from the HFE process or allocating the revenue generated by some taxes on a per capita basis.

23 NSW should seek a direction from the Treasurer's Conference to the CGC to review the possibility of:

- *equalising less than 100 per cent of the difference in standardised per capita tax*
- *removing some (current and future) taxes from HFE consideration*
- *removing some part of each tax from HFE consideration*
- *distributing less than 100% of the general revenue grants through the equalisation pool.*

24 In the calculation of grant relativities, NSW should propose that the current COAG review of SPPs should consider quarantining out SPPs that meet a national objective or are performance based, if such a review is not already on the agenda for COAG.

Ai Group supports Recommendations 19, 20, 21, 22, 23 and 24. We suggest that particularly for Recommendations 19 and 20, NSW could seek for these matters be

included in the scope of the existing Review of the Tax System that has been initiated by the Commonwealth.

In any case, implementation of Recommendations 19 to 24 should be undertaken in close co-ordination with the Review initiated by the Commonwealth.

Managing the Reform Process

Recommendation 25. OFM and OSR should be jointly responsible for implementing the short to medium recommendations for change to the NSW taxation system that are endorsed by the Government. OFM should provide the implementation strategy, and report annually on progress against the strategy in the budget papers.

Recommendation 26. NSW Treasury should allocate funds to enable it to undertake or commission specific research to support future strategic directions for improving the tax system.

Recommendation 27. NSW should pursue further opportunities for the interstate harmonisation of State taxes through an appropriate national forum.

Recommendation 28. NSW should propose that COAG should foster initiatives between States in the area of intergovernmental fiscal arrangements.

Ai Group supports Recommendations 25, 26, 27 and 28.