

A few small steps on a long and difficult journey

The long-awaited release of the Australia's Future Tax System report and the Government's response marks the beginning of what business hopes will be a longer-term process of more significant tax reform.

The Henry Report sets out a blueprint for the tax system in the long term. The Government's first response represents a start but falls short in a number of areas.

Undertaking the Review was a mammoth task involving many arduous hours.

The ambition was not to design the perfect tax system. Rather, we sought to give impetus to the design of one that will work best for Australia, our values and aspirations while meeting the very big challenges Australia faces in the decades ahead. Those challenges will be significant as our population grows and ages, as globalisation makes capital and labour more mobile and with sustainability increasingly shaping our policy options.

The report speaks for itself. Now, the debate will start in earnest about the shape of the reforms which will be implemented and those which will be put in the too hard basket. That debate has now started.

The Government's cautious response to the 138 report recommendations is not unexpected. Embarking on more sweeping tax reform in a pre election environment was always going to be a big ask. However this should not let them, the Opposition or the Senate off the hook.

Business will be looking for more detail on the next phase of reform that follows this initial package, hopefully as soon as next week's Federal Budget.

At the centre of the Government's response is its Resources Super Profits Tax (RSPT).

While the sector directly affected will find this difficult to digest, it is a move in the right direction at a conceptual level. An RSPT is a much more efficient method of levying tax than the current State-based royalties system, which the Government's plan would neutralise. Much of the devil will be in the detail, including the transitional arrangements for existing mining projects. The Government's proposal to consult widely as it designs and implements the new approach is critical, and the success or otherwise of the reform will depend on this.

We welcome the phased reduction in the company tax rate to 28 per cent but it does not go far enough and this is disappointing. The Government should have mapped a definite pathway to a company tax rate of 25 per cent as recommended by the AFTS Report. The Government proposes a two-step reduction – to 29 per cent in 2013-14 and then 28 per cent by 2014-15 – and this will help to claw back some of the ground we have lost in recent years as other countries have lowered their business tax rate.

But consider this - amongst 24 comparable OECD economies, Australia currently has the third highest company tax rate - under these proposed changes we would have the ninth highest, but a more ambitious cut to 25 per cent would put us into the top ten.

There is also reason to be concerned that this reform will hinge upon the Government getting the RSPT proposal implemented. The reduction in the company tax rate is a worthy tax reform objective regardless of whether the proposed RSPT succeeds or flounders.

The Government should be applauded for proposing to invest some of the proceeds from the RSPT into resource related infrastructure, through the creation of a new state infrastructure fund. However, the detail of how this will happen is still scant and somewhat confusing. We already have a Building Australia Fund designed in part to support this type of investment. Under the BAF investments are subject to a rigorous cost benefit analysis. Indeed simply using the existing Infrastructure Australia process would seem eminently more sensible.

Business has deep concerns about the mooted changes to superannuation including the raising of the Superannuation Guarantee to 12 per cent. This is a 33 per cent increase in what it costs employers to fund superannuation for their workers. To adopt this, business will be looking for wages trade-offs similar to those that accompanied the introduction of compulsory superannuation in the early 1990's at a minimum. Productivity in Australia will also have to lift considerably to support such an increase.

For small business, granting them instant write-offs on the purchase of capital assets up to \$5,000 is most welcome. Although less than the AFTS recommended threshold of \$10,000, the small business sector will get a boost from this measure.

There is also a substantial amount of tax reform work left undone. This includes, for example, the removal of existing taxes, the tax treatment of business losses, and administrative reforms.

There is also a very important welfare reform agenda which is central to driving participation and productivity objectives.

Clearly, while the Government's initial response falls short of bold or sweeping long-term tax reform, a pathway to tax reform now exists.

There is plenty of room for a much more ambitious reform agenda in coming years, and the AFTS Report is the blueprint for that.