SUBMISSION TO THE SENATE ECONOMICS LEGISLATION COMMITTEE INTO THE TAX LAWS AMENDMENT (TEMPORARY BUDGET REPAIR LEVY) BILL 2014 AND RELATED BILLS BY TAXPAYERS AUSTRALIA

We welcome the invitation to comment to the Senate Economics Legislation Committee into the proposed Temporary Budget Repair Levy ("Debt Tax").

Taxpayers Australia represents the voice of the Australian taxpayer. Whilst the vast majority of taxpayers will not have to pay the new tax, this tax is part of a broader package of tax and spending measures which affect almost every Australian taxpayer and needs to be considered both in its own terms and as part of that broader package. The purported background to the tax – to help fix the so-called Budget Emergency – also needs to be considered.

Policy Intent behind the Debt Tax

The policy has been sold to the Australian public as part of a strategy to fix the Australian budget which the government projects will reach a deficit of $667bn by 2023-24 unless action is taken to either slow spending, increase revenue or both. The Debt Tax itself is purported to be a mechanism which spreads the pain to higher earning individuals who are largely unaffected by the raft of spending and welfare cuts which bite those on lower incomes. Treasury figures indicate that the tax will raise about $3.1bn over its three year life (or less than $1bn per year), whilst ATO estimates indicate the tax will impact about 290,000[1] taxpayers.

We believe that the tax represents poor public policy. Estimates released by Treasury show public debt accelerating rapidly over the period 2018-2023 but we note that the Debt Tax is scheduled to end in 2017. The $3.1bn which Treasury estimates the tax will raise contributes little to the repair of the budget and contributes nothing in the period when action is most required (post 2017). The modest contribution which the tax imposes on wealthy taxpayers is disproportionately small compared to the heavy lifting being done by those at the opposite end of the wealth spectrum, particularly the sick, the elderly, families with children, students and the unemployed.

The constantly shifting speculation (much of it from seemingly well informed sources) in the days leading up to the Federal Budget suggests that the Debt Tax was designed as a political "fix" to provide cover for the raid on those on lower incomes and suggests also that the final details of the tax were only decided at a late stage with a view to managing political outcomes rather than

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[1] Per the latest ATO tax statistics, for the 2011-12 year, the number of taxpayers in the top tax bracket, ie earning income in excess of $180,000 was 293,540 (or 2.3% out of a population of individual taxpayers of 12,736,030)

economic ones. In short, the tax appears to have been hastily designed, with one eye on opinion polls and little or no thought given as to how the tax would fit into a broader agenda of tax reform or to the basic principles of tax design.

It is clear that if the government was serious about spreading the pain fairly across the community, there are numerous ways in which it could have passed on the burden to the wealthy including but not limited to:

- Removal of tax concessions around negative gearing which would save $4bn per annum in the short term[2]
- Reform of superannuation tax concessions to tax superannuation earnings of those over 60 at 15% which would save $3bn per annum[3]
- Reducing superannuation contribution tax concessions such that only $10,000 can be contributed at the reduced 15% tax rate (currently $25,000) which would save $6bn per annum[4]
- Most obviously of all, permanently increasing the top rate of income tax so that high income earners continue to contribute to the deficit reduction process through the period post 2017

The fact that none of these measures – all of them widely flagged by tax policy specialists over many years – were seriously considered is a clear indication that the government is not serious about spreading the burden and that the Debt Tax itself is camouflage designed to maximise public attention whilst minimising the actual burden on the wealthy.

Design Flaws with the Debt Tax

Based on 2011-12 ATO figures, there is already a thriving industry in wealthy individuals using tax minimisation techniques to avoid the top rate of income tax. Of the 293,540 individuals earning more than $180,000, 18,805 used tax minimisation techniques to reduce their taxable incomes below $180,000. Included in those figures are 75 individuals who earned in excess of $1m but paid no income tax at all.

Clearly, with tax minimisation already thriving in this sector, the increase in the top rate of income tax will lead to an upturn in tax planning, which is likely to directly impact both the numbers of people who pay the Debt Tax and the amount of extra tax which they pay.

Treasury estimates are therefore likely to be overstated because considerable amounts of relatively straightforward tax planning is likely to take place which have the effect of reducing taxable income, often to beneath the $180,000 threshold.

In particular, we note that many taxpayers are likely to adopt one or more of the following strategies in order to minimise or eliminate the effect of the tax increase:

1. In Year One of the levy, they will accelerate the receipt of taxable income from the 2014-15 year (when the tax would apply) into the 2013-14 year (when the tax will not apply), hence reducing taxable income in 2014-15

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[2] The Grattan Institute, Balancing Budgets: Tough Choices We Need, November 2013
[3] The Grattan Institute, as above
[4] The Grattan Institute, as above

2 In Year One of the levy, they will defer tax deductible expenditure from the 2013-14 year into the 2014-15 year, when tax relief will be available at the higher rate, hence reducing taxable income in 2014-15

3 In Year Three of the levy, they will accelerate tax deductible expenditure from the 2017-18 year (when the tax will not – on current proposals – apply) into the 2016-17 year, when tax relief will be available at the higher rate, hence reducing taxable income in 2016-17

4 In Year Three of the levy, they will defer receipts of taxable income from the 2016-17 year (when the tax would apply) into the 2017-18 year (when the tax will not apply), hence reducing taxable income in 2016-17

5 Because the corresponding increase in rates of FBT will not apply until 1 April 2015, employees will take advantage of the 9 month arbitrage opportunity to salary package various benefits, taking advantage of the lower 47% rate of FBT compared to the top 49% rate of income tax.

6 Taxpayers will increase contributions to superannuation funds, taxable at 15%, with a view to reducing their taxable income to below the $180,000 threshold at which the levy will apply.

7 Taxpayers with family discretionary trust structures will plan to split and stream their incomes across the beneficiaries of the trust (eg children and spouses) such that additional income is charged to beneficiaries who pay income tax at the lower rates and the main “breadwinner” reduces their taxable income below the $180,000 threshold.

We note that most of this planning is relatively straightforward and is already being actively marketed by many tax advisers. In short, it is clear that in practice only the wealthy but poorly advised will be paying the Debt Tax.