AUSTRALIAN INDUSTRY

GROUP

Senate Standing Committees on Economics

Minerals Resource Rent Tax Repeal and Other Measures Bill 2013.

Ai Group's Submission

21 November 2013

Introduction

The *Minerals Resource Rent Tax Repeal and Other Measures Bill 2013* proposes the removal of the Minerals Resource Rent Tax with effect from 1 July 2014; it discontinues a number of other measures; and it reschedules the phasing in of the increase in the superannuation guarantee charge to 12 per cent.

In the Treasurer's Media Release of 24 October 2013 announcing the release of the draft legislation, the fiscal impact of the proposed measures was a boost to the underlying cash balance over the forward estimates of more than $13 billion.

Ai Group's comments are focused on the policy case for the measures put forward in the Bill. We are also very mindful of the need for appropriate fiscal discipline and the need to reduce costs on business, lift business investment and reduce regulatory burdens. Further, we are mindful of the Government's foreshadowed review of taxation which will provide an opportunity to examine in greater detail a number of areas of tax policy related to the measures proposed in this Bill.

On the basis of these considerations, Ai Group:

- **Supports** the repeal of the Minerals Resources Rent Tax;
- **Does not support** the repeal of the recently enacted loss carry-back provisions;
- **Supports** the repeal of accelerated depreciation for motor vehicles;
- **Does not support** the proposal to reduce the small business asset write off threshold;
- **Supports** the repeal of the geothermal exploration provisions;
- **Supports** a pause on further changes in the rate of the SGC superannuation guarantee charge (SGC);
- **Supports** the repeal of the low income superannuation contribution; and,
- **Supports** the repeal of the income support bonus and the schoolkids bonus.

While retaining the loss carry back provisions and the current small business asset write off threshold would have near term revenue implications (of an estimated $3.8 billion over the forward estimates), the revenue "lost" is in reality deferred as in both cases the issue is essentially a matter of the timing of legitimate deductions.

Both measures have a strong policy rationale and their retention would boost investment and cash flow to the particular benefit of smaller businesses; to the general benefit of the broader economy; and the commensurate growth of the tax base over the medium term.

Response to the Measures Proposed in the Bill

Ai Group supports the repeal of the Minerals Resources Rent Tax.

- We note however that the fundamental policy case for having a well-designed approach to the taxation of "super profits" associated with high prices received from the sale of non-renewable resources is a strong one.

  If designed well and in a way that only taxed profits in excess of the level that would attract investment, distortions could be minimised and would certainly be lower than those that arise from quantity-based or price-based royalties which are levied regardless of the return on capital employed.

  The role of such a tax should be considered in the Government's foreshadowed review of taxation. The MRRT however was very poorly designed and would not serve as an effective basis on which to build a well-designed approach.

  A key part of this consideration is how best to transfer to a more efficient approach to the taxation of non-renewable resources while not detracting from the fiscal position of the States and Territories.

Ai Group does not support the repeal of the recently enacted loss carry-back provisions.

- There is a strong policy case to have provisions in Australia's income tax arrangements that address the asymmetrical treatment of tax losses. Many other countries have such measures in recognition of the unfairness and the bias against risk taking associated with the asymmetric treatment of losses. These were also the primary motivations behind the recent enactment of the limited loss carry-back measures that this Bill proposes to remove.

  Retaining the recently enacted loss carry-back provisions would serve two important purposes:

  - It would retain the, albeit limited, inroads into the distortions the Australian tax system imparts as a result of the asymmetric treatment of losses; and
  - By giving the taxation authorities a level of experience in the administration of such arrangements, it would better inform the insights they could provide to the Government's foreshadowed review of taxation when it examines this complex area of tax policy.

Ai Group supports the repeal of accelerated depreciation for motor vehicles.

- Selective accelerated depreciation arrangements for motor vehicles used by small businesses distorts small business's investment decisions in favour of expenditure on motor vehicles relative to expenditure on other, and in many cases, more productive assets. To the extent there is a case for special depreciation arrangements for small business, the treatment of cars should be included under a more uniform regime.

Ai Group does not support the proposal to reduce the small business asset write off threshold.

- Reducing the thresholds available under the small business asset write off regime from $6,500 to $1,000 will add complexity and compliance costs for eligible small businesses. It will subtract from their cash flow over the next few years at a time when many small businesses are struggling and it will reduce the return on new investment at a time when there is weak investment outside of the mining-sector.

  Australia's Future Tax System Review recommended an increase in the small business asset write off threshold to $10,000 noting that "this would allow small businesses to immediately write-off most of their asset purchases" and that this would contribute to "a significant simplification for small business".

  If enacted, the short-term gain to the revenue from reducing depreciation deductions will be offset after a few years as deductions deferred by the measure reduce taxable incomes in future years. In contrast the increase in small business compliance costs will be permanent.

Ai Group supports the repeal of the geothermal exploration provisions.

- While the treatment of exploration expenditure is in need of significant improvement, the specific and circumscribed measures that this Bill seeks to repeal would be better considered in the context of the Government's general tax review which can conduct a broader examination of the tax treatment of exploration.

Ai Group supports a pause on further changes in the rate of the SGC superannuation guarantee charge (SGC).

- Lifting the superannuation guarantee was aimed at raising non age-pension retirement incomes. While very supportive of the superannuation system and while we recognise the current gaps in the adequacy of retirement incomes for many people, Ai Group did not support this measure when it was introduced.

  Depending on the incidence of the changes, it imposes costs on business or it detracts from disposable incomes. These impacts are occurring at a time when business costs are under pressure and household spending is weak and, regardless of the economic incidence of the measure, it has dampened economic activity and growth when the economy has been slowing.

In addition to these shorter-term considerations, the selection of this means of raising the adequacy of the superannuation system from a range of alternatives, including the more substantial approach floated in the Australia's Future Tax System Review, was not subject to consultation nor community debate.

Ai Group favours a more considered approach to examining the case for improving the adequacy of superannuation arrangements and the alternative means of doing so. This should be considered in the context of the Government's review of taxation.

Ai Group supports the repeal of the low income superannuation contribution;

- While often referred to as "concessional", current arrangements for taxing superannuation penalise low income earners. In many cases, they impose higher tax rates on superannuation contributions and the income earned in superannuation funds than would apply if those income streams were taxed at low-income taxpayers' marginal tax rates.

  This flaw certainly needs addressing but measures such as the low-income superannuation contribution are patchwork rather than systemic solutions. Ai Group supports a more substantial response to this policy issue which should also be considered in the context of the Government's tax review.

Ai Group supports the repeal of the income support bonus and the schoolkids bonus.

- These measures, while no doubt appreciated by eligible lower and middle income households, amount to a redistribution of $5.7 billion dollars over the forward estimates from an anticipated revenue source that has not materialised. Indexation of these new entitlements would see the cost to the revenue grow further over time.

  The policy case for these additional and widely dispersed transfer payments was never articulated and in its absence the case for continuing them is very weak.

Revenue and Economic Impacts

According to its valuable work on estimating the budget impact on election promises, the Parliamentary Budget Office (PBO) has provided information that can be used to examine the impact of the budget costs of the measures proposed.

Estimated Impact of Ai Group Variations

(underlying cash balance impacts)

Measure	**2013-14**	**2014-15**	**2015-16**	**2016-17**	***Total***
Retaining loss carry back provisions	-	350	300	300	*950*
Retaining small business asset write off provisions	-	850	1,065	990	*2,905*
Total	-	1,200	1,365	1,290	*3,855*

Source: Parliamentary Budget Office

The underlying cash balance impacts of the proposals give an incomplete impression of the actual revenue impacts for two main reasons:

- The Government's proposal to remove these measures would impart a temporary gain for the revenue. That is, the revenue "gain" would be "repaid" to taxpayers over time.
    - In the case of asset write-off measure, the depreciation deductions are just postponed so that future depreciation deductions are greater than they would be if the Government has not reduced the asset write-off threshold.
    - With the loss carry back provisions, the removal of the measures would also see the removal of the compensating adjustment in franking accounts and, further, the loss would be claimed back in the future when the business returns to profit.
- Secondly, the PBO's approach does not take into consideration the indirect impacts on business cash flows and investment that the removal of these measures will impose. After all, the figures in the table above represent a transfer from smaller businesses to the government in these years – a transfer of over $3.8 billion. The contribution of the small business sector to the growth of the economy and of the tax base will be correspondingly lower than it would be if the measures were retained.

While the impact on small businesses of these measures over time is overstated by these data because the measures relate to the timing and not the quantity of deductions, the figures above nevertheless give a realistic picture of the near-term impact on the small business sector at a time when the economy generally is sluggish and investment is weak.