



## THE TAX INSTITUTE

15 March 2013

Dr Warren Mundy  
Presiding Commissioner  
Small Business Study  
Productivity Commission  
GPO Box 1428  
CANBERRA CITY ACT 2601

By email: [small.business@pc.gov.au](mailto:small.business@pc.gov.au)

Dear Dr Mundy

### **Regulator Engagement with Small Business – Tax Institute submission**

The Tax Institute is pleased to have the opportunity to make a submission to you in relation to the Productivity Commission's study into *Regulator Engagement with Small Business*.

The Tax Institute is Australia's leading professional association in tax, with more than 11,000 tax practitioner members. Further details about The Tax Institute are included at Appendix A.

#### *Context*

The Tax Institute has a significant history of involvement and interest in taxation issues that affect taxpayers in the small to medium business ('**small business**') sector. Our interest is two-fold: a significant percentage of our membership provides advice to taxpayers in this sector and, in addition, many of our members also operate small businesses themselves.

As such, our membership has significant interest in both tax reforms that are aimed at assisting small business as well as other tax-related regulatory matters that impact on small business.

#### *Tax-related issues affecting small business*

From a tax perspective, The Tax Institute has significant interest in a range of matters that affect small business, such as:

- Ensuring Australian Taxation Office ('ATO') practices and procedures do not impose an undue burden on or cost for small business;
- The appropriateness of current tax policy settings intended to support small business, and resulting regulatory requirements;
- Ensuring small business issues and concerns are represented in tax-related consultation with Government and are not subsumed by larger business interests (as small businesses often lack the available resources to consult with Government independently);
- Ensuring the significant work that remains to be undertaken in respect of simplifying existing tax laws to alleviate the compliance burden on small business continues. In this regard, we note that compliance costs are regressive in their impact on small business;
- Exploration of the possibility of creating a separate small business entity structure through which small business can operate and which amalgamates the benefits of existing, available structures (such as company, trust, partnership and sole trader structures) (see further discussion below);

We have of course been broadly supportive of the Government's recent small business tax reform agenda, such as the instant-asset write off and limited tax loss carry-back.

Nevertheless, it is worth noting that the potential benefits of such reforms still pale in comparison to the efficiency benefits that would stem from cleaning-up and streamlining areas of the tax law that result in significantly increased compliance costs due to their complexity. Notably, such compliance costs are regressive in their application to small business. Relevant areas of the tax law include:

- Taxation of trust income;
- Current problems with Division 7A of the Income Tax law (currently under examination by the Board of Taxation);
- Complicated small business entity tests (including grouping rules designed to counter tax-avoidance but which mostly cause complexity);
- Personal services income rules;
- Superannuation contributions restrictions (especially relevant if you need to contribute the gain from the sale of a business into Superannuation to get small business CGT concessions);
- Transfer pricing rules (on which we have advocated for an increased *de minimus* rule and decreased record keeping requirements for small business); and
- Payroll tax (including grouping rules designed to counter tax-avoidance but which mostly cause complexity).

Furthermore, some benefits within the tax law are almost off-limits to small business due to the complexity of the rules and the prohibitive cost of obtaining sophisticated tax advice to ensure the correct tax outcomes are achieved (for example; tax consolidation, share buy-backs, and certain fringe benefits tax concessions).

We submit that there should be a focus on:

- Streamlining definitions and access to small business concessions where possible;
- Greater harmonisation between small business definitions in State and Federal tax laws;
- Simplifying existing tax laws especially in the areas set out above including via the Board of Taxation where possible; and
- Providing greater resources to organisations such as the Inspector-General of Taxation that assist in identifying areas in which ATO processes and interactions with small business can be simplified.

#### *Creation of a separate small business entity structure*

The Tax Institute also has a particular interest in an 'entity-flow through' proposal on which Treasury has consulted with members of the ATO's Small Business Consultative Group. As mentioned above, this is part of exploring the possibility of creating a separate small business entity structure.

At the same time as considering the benefits of a consistent definition of small business, the Government could give consideration to entity flow-through treatment in the context of the creation of a separate small business entity structure.

Our members are broadly of the view that the proposal warrants further investigation and consideration, and could be constructed as a sufficiently attractive alternative to allow the consolidation/removal of existing, complicated ownership structures.

Nonetheless, it is our view that the proposal requires significant development and would benefit from wider exposure and consultation, as well as industry and private sector input, including potentially via the Board of Taxation.

An entity flow-through treatment for gains and losses would bestow many of the benefits currently available via the use of a trust with relatively little compliance costs. Such a structure may also counter some of the ATO's current integrity concerns with the use of trusts. If such a structure also allowed the optional retention of income at the corporate tax rate, it would allow almost all of the benefits that can currently be obtained via use of a company and discretionary trust via a cheaper and simpler to administer vehicle. The acceptance of such a structure would depend on the allowance of rollovers to defer the realisation of gains and obviate stamp duty liability on adoption of the structure.

Entity flow-through treatment could also offer reduced compliance costs if small businesses were able to structure their businesses through a single simplified structure rather than continue to use a collection of entities so commonly used to structure small businesses.

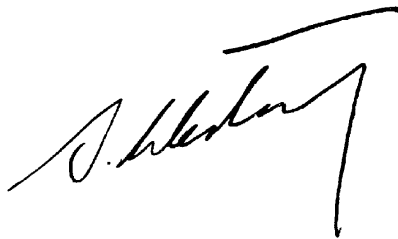
If the new entity structure offers currently available advantages, it should not result in a significant cost to the revenue, and will offer a unified set of data on the tax attributes of the small business sector that will prove advantageous in policy decision making. If such a structure eventually makes possible the eradication of other entity choices in the small business sector, taxpayers and the revenue authority alike will stand to benefit from a simplified mode of operation.

We note that the flow-through of losses would allow for greater symmetry in the tax treatment of losses but would be inconsistent with the optional retention of profits at the corporate tax rate. We are broadly supportive of elective flow-through of losses, but are cognisant that such a change will raise integrity concerns that may also need to be countered.

Pending the outcome of this study, there may be value in the Government further examining an entity flow-through regime and separate entity structure for small business.

Should you have any queries with respect to any of the matters raised above, please do not hesitate to contact either me or Senior Tax Counsel, Robert Jeremenko, on 02 8223 0011.

Yours sincerely

A handwritten signature in black ink, appearing to read 'S. Westaway', with a long horizontal stroke extending to the right.

Steve Westaway  
President

## **APPENDIX A**

### **About The Tax Institute**

The Tax Institute is Australia's leading professional association in tax, with more than 11,000 tax practitioner members. The Tax Institute sets the benchmark for the most up-to-date tax professional development events and education programs in the country. This means that members of The Tax Institute are best placed to have the highest level of expertise in the field.

The growing membership base includes tax professionals from commerce and industry, academia, government and public practice throughout Australia. The Tax Institute's reach now extends to over 40,000 Australian business leaders, tax professionals, government employees and students through the numerous specialist, practical and accurate tax publications – all of which ensure that the latest information is available at their fingertips.

Established in 1943, the purpose of The Tax Institute was to provide education and information products and services to the tax profession as well as support improvements in the tax law and its administration. That core purpose remains.

Today we lead the tax profession with a strong and authoritative voice in supporting a fair and equitable tax system in Australia, whilst at the same time providing a full suite of education and information products that keep today's tax professional up-to-date and build the capacity of the next generation of tax professionals.

[www.taxinstitute.com.au](http://www.taxinstitute.com.au)

[www.twitter.com/taxinstituteoz](https://www.twitter.com/taxinstituteoz)

[www.taxinstitute.blogspot.com](http://www.taxinstitute.blogspot.com)