THE TAX INSTITUTE

THE MARK OF EXPERTISE

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2015-16 Federal Budget Submission

12 March 2015

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Budget Policy Division
Department of the Treasury
Langton Crescent
PARKES ACT 2600

Attention: Mr Claudio Damiani

By email: prebudgetsubs@treasury.gov.au

Dear Mr Damiani,

2015-16 Federal Budget Submission

The Tax Institute is pleased to respond to the invitation from the Treasurer, The Hon Joe Hockey MP, to submit our views with respect to priorities for the 2015-16 Budget.

We note that the Treasurer has advised that the Budget will 'continue the Government's commitment to repair the budget, to ensure the Commonwealth lives within its means, pays down its debt and maintains a credible path to surplus[1]'. There is also a Government commitment to 'productivity-enhancing investment and reform to build a stronger and more prosperous economy[2]'.

We welcome these commitments and trust that this submission will assist in identifying opportunities to improve tax policy outcomes for all Australians.

Tax and Federation White Papers

The Government is shortly expected to commence the White Paper process on the Reform of Australia's Tax System. We welcome the White Paper process as it is crucial to achieving a longer-term considered approach to tax reform. The Government has also agreed to work with the States and Territories on the development of a White Paper on the Reform of the Federation. These two White Papers must be developed concurrently given the significance of the Federation to the structure of Australia's tax system.

[1] The Hon Joe Hockey MP, Media Release, 18 December 2014
[2] As above

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Given the separate Tax and Federation White Paper processes, this Budget Submission focuses only on those matters that The Tax Institute believes should be considered in the context of the 2015-16 Budget, rather than in the longer-term White Paper process, which will be the subject of separate submissions.

About The Tax Institute

The Tax Institute is Australia's leading educator and professional association in tax, with more than 15,000 members. Further details about The Tax Institute are included at Appendix A.

Context

The Tax Institute continues to advocate for the Government to provide a sustained commitment to tax reform for the benefit of all Australians. This requires a measured and structured approach to reform, that includes a timeline and a process for advancing priority issues.

Despite Australia's budgetary position, it is crucial that we do not delay the hard work on policy formulation that is required to improve our tax and transfer system. To ensure that the country is well positioned for the challenges of the decades ahead, Australia must do the preparatory work now to ensure the tax reform debate continues and that there is a plan for reform in the coming years as our budgetary position improves.

The benefits of tax reform will flow to all Australians in the form of a stronger economy.

Australia's tax and transfer system must strive to be efficient, equitable and simple. The system should encourage savings and investment as well as greater workforce participation, particularly having regard to the ageing of our workforce. The revenues generated by the system should be sufficient to meet public and social needs, in turn supporting economic growth. In addition, it is important that the superannuation system provides Australians with access to a minimum standard of living in retirement.

The Tax Institute has formulated a set of Tax Policy Principles that serve to guide thinking about Australia's tax system and possible reforms; the principles are at Appendix B.

As recognised in *Australia's Future Tax System Review* (the Henry Review), tackling the economic, demographic and environmental challenges that face Australia over the medium to longer term require planning and commitment today.

In this context, below is a summary list of issues and recommendations that The Tax Institute considers should be a priority for the Government to consider in the 2015-16 Budget; this list is not in any particular order. These issues are discussed in further detail at Appendix C.

Priorities for the 2015-16 Budget

Company tax reform

The Tax Institute supports reducing the company tax rate in the medium term from its current 30% to the 25% recommended by the Henry Review. The Government's announced 1.5% reduction for the year ended 30 June 2016 is a step in the right direction. The Tax Institute would encourage the Government to pursue cutting the company tax rate for all companies, not just small business companies.

Multinational taxation

The Tax Institute supports the Government's commitment to addressing base erosion and profit shifting in conjunction with Australia's G20 partners as signalled by its endorsement of the OECD's Action Plan on BEPS in July 2013. We support Australia's involvement in this work and in particular, the work in the area of the digital economy to address the gaps that exist that allow for double non-taxation, that is, income wherever sourced not being appropriately taxed in any jurisdiction. Australia should be involved in the outcome of the OECD's work in this area to ensure that income derived by multinational corporations in particular is subject to an appropriate level of taxation. This is not an issue that Australia can nor should address alone.

Tax transparency

The Tax Institute is broadly supportive of efforts to increase transparency. However, we consider there is significant risk where the publication of selective information related to a particular taxpayer's tax position may be misinterpreted. The publication of the information required under Australia's tax transparency laws in the absence of appropriate context is likely to misinform the public if not properly managed once it is in the public domain. It remains to be seen what deterrent effect publication of this information will have.

Small business

The Government must continue the significant work that remains to be undertaken in respect of simplifying existing tax laws to alleviate the compliance burden on small business. We support the Government's efforts to address the compliance burden through the Board of Taxation's fast-track review into *Tax System Impediments facing Small Business* conducted in 2014. However, there is still work to be done in this area, including implementation of the Board's recommendations; exploring the possibility of creating a separate 'small business entity' structure; streamlining access to small business concessions; and simplifying carry-forward loss integrity measures.

Superannuation

The Tax Institute sees potential for deregulation in the superannuation sphere in measures including the repeal of the '10% rule'.

Announced but un-enacted tax measures

While we welcome moves by the Government to continue to clear the un-enacted measures backlog and prioritise the remaining un-enacted measures, it is imperative that the Government continues to monitor announced measures in future to ensure that a backlog does not develop again. The prioritised measures should be legislated as soon as possible.

Relevant Government agencies, including the Department of the Treasury and the Office of Parliamentary Counsel, should have sufficient resources dedicated to both implementing these measures and preventing any future backlog.

Deregulation

The Tax Institute supports the Government's continued deregulation initiative and the publishing of a regulation impact statement in respect of each tax reform. However deregulation should not be at the expense of sound reform in areas such as regulation of financial advisers providing tax advice.

Child care affordability

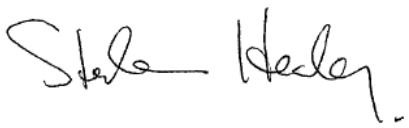
There are many women who would participate in the workforce except for the unavailability of child care. In many cases these individuals would earn higher wages than the wages of the child care workers and be able to make contributions to their superannuation funds. Two options for improving access to child care through the tax system would be to allow a tax deduction for child care costs and to use a refundable tax credit or cash grant.

Budget 'lock-up'

Finally, The Tax Institute would welcome another invitation to participate in the Treasury stakeholder 'lock-up' on Budget night, 12 May 2015. Given that our 15,000 members throughout Australia (including small rural and suburban accountants, senior members of the bar specialising in tax and tax practitioners servicing large corporations) rely upon our report of key Budget measures affecting their clients, it is crucial that we are able to report this in a timely manner.

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

Yours sincerely



Stephen Healey
President

APPENDIX A

About The Tax Institute

The Tax Institute is Australia's leading professional association and educator in tax, with more than 15,000 members. We set the benchmark for the most up-to-date tax professional development events and education programs in the country. Meaning our members are best placed to have the highest level of expertise in the field.

Our growing membership base includes tax professionals from commerce and industry, academia, government and public practice throughout Australia.

In 2012, we introduced the internationally recognised Chartered Tax Adviser (CTA) designation to ensure our members have the credentials to demonstrate their tax expertise to employers and clients.

In 2014, we became accredited as a higher education provider and introduced the Graduate Diploma of Applied Tax Law, which has been designed to meet the changing needs of the tax profession.

Our reach 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
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APPENDIX B

Tax Policy Principles

- Tax laws exist primarily to generate revenue to aid the function of Government and the provision of Government services.

- Tax laws may also fulfil the function of either encouraging or discouraging certain activities, as defined by Government.

In fulfilling these goals, our tax system should:

1. Meet the Government's revenue needs.

2. Consider these revenue needs in a broader and longer-term context of current and future Government services, anticipated demographic changes, the specifics of our economy (such as heavy Australian reliance on foreign capital).

Efficiency

3. Minimise distortions wherever possible, unless intended. This means minimising special treatments, exemptions and cliffs in the tax system (especially in relation to substantive tax provisions) where possible.

4. Encourage or discourage only those behaviours that are intended to be affected.

5. Support growth, productivity (including workforce participation), investment and desired social outcomes (such as equity).

6. Tax entities (companies, trusts, partnerships) as conduits.

7. Tax individuals, superannuation funds and not-for-profits as ultimate taxpayers.

8. Seek to tax the substance of the transaction appropriately, but only via clearly defined laws rather than the inclusion of nebulous concepts in legislation.

9. Levy taxes on a uniform base where possible (for example, current taxes on the factors of production: land tax and payroll tax).

10. Levy taxes on the basis of a broad base, low rate principle.

Equity

11. Be horizontally equitable in relation to each type of final taxpayer. Integrity provisions may be necessary to safeguard equity and prevent specific taxpayers from taking advantage of current laws.

Simplicity

12. Be simple to understand and apply, unless the desired outcome can only be achieved via complexity and after taking the cost of that complexity into account.

13. Resolve integrity concerns commensurate with risk to revenue/risk to integrity.

14. Minimise compliance costs for both taxpayers and the ATO.

15. Rely on safe harbours and sound administration/interpretation rather than blunt legislative instruments where possible without jeopardising the rights of taxpayers or the rule of law.

Other

16. Be formulated with reference to the current structure of the system, including taxation (including state taxation), offsets, transfers and other Government payments.

17. Be formulated with reference to, and after proper consultation with, the relevant stakeholders, including taxpayers, the revenue authority, the Inspector-General of Taxation and other relevant agencies.

18. Cost measures in line with an objective standard, and also with reference to likely behavioural changes by individuals, investors, businesses etc.

19. Be altered prospectively only, unless retrospective application would not be adverse to taxpayers or retrospectivity is necessary to protect the integrity of the tax system.

20. Changes should be legislated as soon as possible after announcement, subject to the need for consultation. This is especially so if the measure applies from date of announcement or earlier.

21. Not be altered unless necessary. If necessary, should be altered in line with the principles set out above.

APPENDIX C

The Tax Institute
2015-16 Federal Budget Submission

Context

The Tax Institute continues to advocate for the Government to provide a sustained commitment to tax reform for the benefit of all Australians. This requires a measured and structured approach to reform, that includes a timeline and a process for advancing priority issues.

Despite Australia's budgetary position, it is crucial that we do not delay the hard work on policy formulation that is required to improve our tax system. To ensure that the country is well positioned for the challenges of the decades ahead, Australia must do the preparatory work now to ensure the tax reform debate continues and that there is a plan for reform in the coming years as our budgetary position improves.

The benefits of tax reform will flow to all Australians in the form of a stronger economy.

Australia's tax and transfer system must strive to be efficient, equitable and simple. The system should encourage savings and investment as well as greater workforce participation. The revenues generated by the system should be sufficient to meet public and social needs, in turn supporting economic growth. In addition, it is important that the superannuation system provides Australians with access to a minimum standard of living in retirement.

As recognised in *Australia's Future Tax System Review* (the Henry Review), tackling the economic, demographic and environmental challenges that face Australia over the medium to longer term require planning and commitment today.

Company tax rate

The Tax Institute supports the reduction of the company tax rate in the medium term from its current 30% to the 25% recommended by the Henry Review. In addition to increasing Australia's attractiveness as a destination for foreign investment, a 25% rate is comparable to rates in similar sized Organisation for Economic Co-operation and Development (OECD) countries. The Government's announced 1.5% reduction for small business from 1 July 2015 is a step in the right direction. However, The Tax Institute would encourage the Government to pursue a cut in the company tax rate for all companies, not just small business companies.

A wealth of reliable evidence indicates that the incidence of company tax falls on employees. This means that reducing the burden of company tax is expected to result in companies passing on the benefits to their employees either in the form of increased wages or additional recruitment – increasing productivity and employment.

A company tax cut would also reduce taxes on investment, increasing the incentives for savings and capital as well as innovation and entrepreneurship – all outcomes that are indisputably in the interests of all Australians. Such a cut would also reduce the incentive for profit shifting out of Australia, allowing us to retain a greater share of the profits generated here in Australia.

Multinational taxation

The Tax Institute recognises that the integrity of the tax base is essential to making a lowering of the company tax rate possible.

In this regard, we welcome the Government's commitment to addressing base erosion and profit shifting in conjunction with Australia's G20 partners as signalled by its endorsement of the OECD's Action Plan on "base erosion and profit shifting" (BEPS) in July 2013. An internationally co-ordinated effort to tackle tax avoidance and re-examine the relevance of existing source and residence doctrines of international taxation is essential to ensure that Australia's international tax system and treaty network adequately address the challenges posed by the increasingly digital international economy and levy taxation on the economic substance rather than form of the transaction.

Consideration of the current activities of multinationals and any proposed changes to tax laws need to take into account the challenging and competitive circumstances faced by businesses operating in an international environment. The effect of such changes in tax laws on inbound investment and potential flow-on ramifications of changes in tax treatment by our trading and treaty partners of outbound investment need to be appropriately taken into account. Businesses should be kept informed and consulted as specific measures are proposed.

On a domestic level, we support the ongoing monitoring of Australia's bilateral treaty network and domestic tax transparency measures discussed below.

The adequacy of Australia's current laws

Australia is renowned for having one of the most complex and robust tax systems in the world. This complexity creates great difficulty for taxpayers to navigate their way through the system to determine what their obligations may be under the Australian tax law. However, the robustness serves to markedly reduce the opportunity for a taxpayer to not comply with their obligations.

Australian registered corporations are incentivised to pay corporate income tax in Australia as a result of the operation of Australia's dividend imputation system. This positively influences tax revenue collection from Australian corporate taxpayers and therefore assists to increase revenue collection in Australia, given that corporate income tax paid is effectively a "forward payment" of income tax payable by shareholders.

Australia has most recently seen a further tightening of aspects of its tax laws to target tax avoidance directly and indirectly, which apply to both Australian registered corporations and multinational corporations operating in Australia. This has included changes to its general anti-avoidance provisions[3], and in respect of international dealings, a tightening of its thin capitalisation rules[4] and new transfer pricing rules[5]. The changes to the transfer pricing rules have resulted in

[3] Part IVA of the *Income Tax Assessment Act 1936* (Cth) (**1936 Act**)
[4] Division 820 of the *Income Tax Assessment Act 1997* (Cth) (**1997 Act**)
[5] Division 815 of the 1997 Act

Australia having some of the most far-reaching powers in the world under its transfer pricing laws, in particular the reconstruction power[6].

We note recent media reports have suggested that large corporations (whether Australian or multinational) are not paying "their fair share of tax". This view is misleading in that it does not reflect that many of these corporations are operating in full compliance with the Australian tax law and meeting all of their obligations under the Australian tax law and is based on a great deal of inaccurate and misleading information that has been published during the past year. We recognise that there may be some instances where inappropriate tax outcomes are obtained. Generally this arises where the interaction between the tax rules of different countries leaves opportunities for income to remain untaxed.

However, statements made in the media suggesting certain groups of taxpayers are not meeting their tax obligations unduly undermines the integrity of the Australian tax system as a whole and in turn erodes the trust and confidence of the public in the tax system. It creates the perception that large corporations, and in particular multinational corporations, are largely non-compliant with their Australian tax obligations and the tax system is unable to curb such behaviour. It is difficult for the administrator of the tax system, the Australian Taxation Office (ATO), to dispel this misconception that is being perpetuated and unfairly tarnishes the reputation of compliant taxpayers in this sector.

Currently, there are co-ordinated efforts by the OECD countries to address BEPS, a concern that has been widely acknowledged by OECD countries, including Australia. We support Australia's involvement in this work and in particular, the work in the area of the digital economy to address the gaps that exist that allow for double non-taxation, that is, income wherever sourced not being appropriately taxed in any jurisdiction. Australia should be involved in the outcome of the OECD's work in this area to ensure that income derived by multinational corporations in particular is subject to an appropriate level of taxation. This is not an issue that Australia can nor should address alone.

Tax transparency

Taxpayers have a legal obligation to meet their tax liability in any jurisdiction in which they operate. It is the duty of a tax adviser to assist a taxpayer to identify these obligations. We observe that Australia's corporate taxpayer sector is largely compliant with their Australian tax obligations and the ATO's own compliance modelling recognises this.

Despite this, Australia has recently expanded its tax secrecy and transparency provisions to impose greater transparency in Australia's corporate tax system. The amendments to the provisions require the Commissioner to publish select information about corporate tax entities that generate total annual income of $100 million or more[7]. This includes publication of:

- the corporation's name and ABN;
- total income;

[6] Section 815-130 of the 1997 Act

[7] Section 3C of the *Taxation Administration Act 1953* (Cth) (**TAA**)

- taxable income or net income; and
- income tax payable

per information the corporate tax entity has disclosed in their income tax return.

The provisions first apply to the 2013-14 income year for which some corporate tax entities may not lodge an income tax return until July 2015. It is anticipated that the Commissioner will first publish the required information in late 2015 following the expected lodgement of all tax returns by affected taxpayers.

It is considered that a significant risk exists that publication of selective information related to a particular taxpayer's tax position may be misinterpreted as these numbers alone are not necessarily indicative of the substantial amount of information that may sit behind them (such as availability of tax losses to reduce assessable income, and amounts added back or subtracted to determine taxable income, each of which can produce a taxable income or net income that significantly differs from total income).

Recent media reporting of 'numbers' related to a particular corporation's tax position in the absence of significant qualitative and quantitative information that informs those numbers can (and has) lead to misinformation. This in turn can lead to the (uninformed) public forming incorrect assumptions about whether a particular taxpayer is meeting its tax obligations. Consequently, this can (and has) undermined confidence in the integrity of the tax system if (and where) the public mistakenly perceives certain taxpayers are not meeting their tax obligations and are not paying their "fair share of tax".

Consequently, the publication of this information can be a 'double–edged sword' – both providing information about a corporate entity's tax position and potentially enabling the information to be misused to misinform the public – and so needs to be carefully managed once in the public domain.

Any publication or discussion of numbers needs to be contextualised with relevant information that informs those numbers to ensure a correct understanding can be conveyed in the public domain.

Additionally, it is not self-evident how useful the publication of particular numeric information alone will be to deter corporate tax entities from engaging in tax avoidance and providing assurance to the wider public these entities are fully complying with their Australian tax obligations. With the first publication by the ATO of relevant information of certain corporates unlikely to occur until late 2015, the deterrent effect of the current transparency rules remains to be seen.

In order to protect the confidentiality of tax information of individuals and small businesses, the tax transparency threshold should be set so as to exclude as many closely held companies as possible, and at total income (as per the relevant income tax return tab) of $250 million rather than the current $100 million.

We consider it important to exclude as many closely-held companies as possible because the disclosure of tax information of closely held, potentially wholly-domestic companies is inappropriate and risks inadvertently disclosing details of some of the tax circumstances of the ultimate individual

owners. In implementing the tax transparency objective, the need to protect the actual and in principle privacy of individual taxpayers needs to be carefully considered.

Small business

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

- The appropriateness of current tax policy settings intended to support small business, and resulting regulatory requirements;
- Ensuring the continuation of the significant work that remains to be undertaken in respect of simplifying existing tax laws to alleviate the compliance burden on small business. 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 (i.e. the company, trust, partnership and sole trader structures);
- Streamlining access to small business concessions where possible;
- Simplifying carry-forward loss integrity measures (the 'continuity of ownership test' and the 'same business test') in order to allow greater flexibility in capital raising and changes in business practice/operations. In this regard we note that a critical issue is the need to minimise the compliance burden and costs associated with complex integrity measures; and
- Providing greater resources to organisations such as the Inspector-General of Taxation which assist in identifying areas in which ATO processes and interactions with small business can be simplified.

We support the Government's efforts to address the compliance burden small business taxpayers face through the Board of Taxation's fast-track review into *Tax System Impediments facing Small Business* conducted in 2014. However, there is still work to be done in this area, including implementation of the Board's recommendations, which mainly focused on administrative changes, and a more in-depth review of relevant areas of the tax law as noted above.

Superannuation

Given the Government has consistently pledged "not make any unexpected detrimental changes to superannuation", The Tax Institute assumes that no significant changes will be made to superannuation in this budget. That includes the retention of the Government's commitment to increase the superannuation guarantee rate to 12%.

The Tax Institute also understands that the structure of the superannuation system (both from a regulatory and taxation point or view) will be considered in the Government's upcoming Tax Reform White Paper. The Tax Institute will therefore defer any comments in relation to larger structural issues relating to the superannuation system to its submission to the White Paper.

Consequently, The Tax Institute has confined this budget submission in relation to superannuation to areas where it considers immediate action is required to "reduce red tape". This includes:

1. Providing a "safe harbour" for the terms of related party limited recourse borrowing arrangement ('LRBA') loans entered into by superannuation funds. The ATO has taken the view that a "non-commercial" LRBA loan triggers the application of the non-arm's length income rules. The ATO has also indicated, in order to establish that the LRBA loan is on commercial terms, that related party LRBA loans must be benchmarked against what is available on the market (and that such benchmark material must be retained by the SMSF trustee). The Tax Institute supports the position that related party LRBA loans should be on commercial terms, however, it is concerned that the benchmarking requirement is often difficult in practice to achieve given the various loan arrangements on offer with different terms and conditions. It is therefore too onerous on taxpayers and can lead to uncertainty. The Tax Institute recommends that "safe harbour" provisions be introduced, setting out certain terms under which a related party can lend to an SMSF without triggering the non-arm's length rules. For example, the safe harbour rules could set out a minimum interest rate.

2. Reforming penalties for employers in relation to the superannuation guarantee system where the failure to pay the amount within 28 days of the end of each quarter has such severe consequences. Even where a worker requests to have the amount paid to them as a contractor, where the failure results from a technical position such as whether a contractor should be treated as an employee, the employer can be liable for large amounts, have multiple levels of penalty and no deductions for the charge amounts. Furthermore, the calculation rules can be complex such as what is to be included in ordinary time earnings ('OTE') as certain items are included and some are not.

3. Allowing greater flexibility for obtaining (or retaining) complying status for SMSFs where a member transfers residency overseas and then returns to Australia seeking to become a resident SMSF again. A simple change that we favour is the removal of the active member test as the test can result in an outcome where a fund loses its compliance status because a member contributes while a non-resident even where they retain strong connections to Australia. The basis of this rule is presumably to limit use of superannuation taxation rules to those without a strong connection to Australia. The other tests for residency already in our view establish that connection.

4. Similarly, the rules allowing migrants coming to Australia with funds in overseas super funds to bring those overseas savings into the Australian super system should be simplified. These measures will increase Australia's competitiveness by ensuring that superannuation is not a barrier to preventing the inbound and outbound movement of people in an increasingly mobile world. Also, Australia should benefit from the increased savings that should flow into Australia rather than being 'stuck' overseas due to the tax impost that would otherwise apply on bringing the money to Australia.

5. Consideration of increasing the contribution caps for persons over 50 (many who have not accumulated much due to broken work patterns or being lumbered with family costs and no prior savings potential).

6. Allowing members aged 65 plus to make contributions without having to satisfy any gainful employment test. Currently this test requires them to work 40 hours in 30 consecutive days. Often this test is satisfied in a somewhat artificial manner or it may be more easily satisfied by those who have a family business. This is leading to distortions as, more and more people are working beyond 65 years given longer life expectancies, rising costs of living, lower real returns on investments and to sustain their lifestyles.

7. Allowing people aged 75 and over to make contributions where they have a limited balance in super. Although this may be an issue that could be considered in the tax white paper, The Tax Institute encourages the Government to consider some flexibility to be introduced in the interim.

8. Abolishing the "10% rule" for personal concessional contributions. This rule creates considerable red tape, is complex and is no longer applicable given our current system. We discuss this point in further detail below and would be pleased to expand on any of the above points if and when needed.

Detailed submission on the reasons for the abolition of the 10% test

Given that the ATO is currently, through the Superannuation Industry Relationship Network, reviewing the application of the 10% rule, the following is an extended explanation as to why the rule should be abolished.

The Tax Institute sees potential for deregulation in the superannuation sphere in repealing section 290-160 of the *Income Tax Assessment Act 1997* (the 10% rule). The 10% rule should be repealed as it is out-dated, discourages saving via superannuation by the self-employed, and creates unnecessary complexity and inequity. This rule should be reconsidered as a matter of priority.

By repealing section 290-160, a taxpayer will be entitled to claim a tax deduction for their personal superannuation contributions irrespective of their employment status – whether employed, self-employed or both employed and self-employed. The control mechanism for the tax deduction will then simply be the concessional contribution cap applicable to the taxpayer.

The 10% rule refers to the limitation of deductions for superannuation contributions for self-employed Australians who earn less than 10% of their earnings from employee activities. Currently, an employee who earns more than 10% of their earnings from employee activities is generally limited to the minimum superannuation guarantee level of support (currently 9.5%) based on their salary and wages.

The 10% rule costs a considerable amount to administer and requires significant documentation to be completed, neither of which add any value. Superannuation funds would be saved an unnecessary cost and impediment if this rule was repealed. The Cooper Review adopted and confirmed the Henry Review recommendation that legislation should be amended to remove trustee administrative burdens that are identified as unnecessary.

The 10% rule was originally introduced in light of factors that are no longer relevant, including the fact that previously contribution limits operated on a per employer / contributor basis, rather than per individual. The 10% rule was a mechanism to ensure that individuals earning substantial passive income as well as employment income didn't benefit from double super contributions. This policy rationale is no longer relevant since the removal of employer / contributor based deduction limits in mid-2007. Since these changes, the superannuation rules now rely primarily on contribution caps per individual, which apply in the same way to the self-employed (and unemployed) compared to employees.

The 10% rule should be removed to encourage the self-employed (and other eligible taxpayers) to contribute towards their own retirement in a timely and sustainable fashion, that is, throughout their working lives. Without this change, there is little incentive for a self-employed or unemployed taxpayer to contribute voluntarily towards their own retirement funding. There is also a category of taxpayers who through no fault are unable to make concessional contributions and may in fact have no employer support as they may not meet superannuation guarantee requirements due to small amounts of salary and wage income.

Furthermore, the current rule also prevents many self-employed from taking full advantage of their concessional contributions cap. The rule results in an arbitrary limit which is inequitable and discourages voluntary contributions as no deduction exists when the 10% rule is breached and such taxpayers fall outside the bounds of the co-contribution scheme.

A number of employment situations result in the need to consider the 10% rule (and therefore resulting in the predictable behavioural responses of reduced contributions and workforce participation). For example, a doctor who gains a visiting medical officer role at a hospital can easily lose their entire ability to claim for a superannuation contribution if they exceed the 10% rule. This makes it harder, especially for regional and country hospitals, to gain valuable input from the self-employed. Another example is where individuals move in and out of employment and self-employment arrangements during a financial year (often typical with those who work on short term contracts and projects).

As the contribution cap is an individual taxpayer limit, there is no longer a requirement to restrict individuals from the ability to make personal contributions to superannuation and claim a deduction. Whether they salary sacrifice from employment or make contributions and claim a deduction, they are limited to total contributions of $30,000 / $35,000 before there is an excess, making the 10% rule inappropriate.

Announced but un-enacted tax measures

We welcome further action undertaken by the Government to clear the un-enacted measures backlog and prioritise the remaining un-enacted measures. Some of the un-enacted measures have been legislated, though there are still many to enact.

All taxpayers require certainty in the identification and scope of tax laws that frame both the obligations to be observed and the liabilities which are to be paid. This includes both prevailing tax

laws as well as proposed changes, regardless of the date on which the announced changes are to take effect.

Such certainty is essential to the proper functioning of our tax system for a variety of reasons, including the need to allow:

- taxpayers to self-regulate behaviour in order to minimise tax risk;
- the fostering of voluntary and informed compliance with tax laws;
- taxpayers to make investment decisions and strike commercial bargains with certainty as to the tax cost resulting from the relevant transaction;
- corporate taxpayers to make informed dividend policy decisions; and
- listed companies to produce timely financial statements that accurately reflect their tax expense.

Accordingly, the remaining prioritised un-enacted measures should be legislated as soon as possible.

We acknowledge the role the ATO has played to provide administrative solutions where possible in place of proposed legislative amendments not proceeding, though this should not become normal practice.

Rather, in future, the Government should limit the practice of announcing an application date for legislation that precedes the date it is introduced into Parliament. While it will sometimes be necessary to announce that a legislative change will apply from the date of the announcement, particularly if the legislative change is an anti-avoidance measure or a change that is beneficial to taxpayers, the Government's default position should be that new measures take effect no earlier than the date the bill is introduced into Parliament. The previous Government would have avoided the legislative backlog if it had adopted this practice.

The Government should also continue to monitor announced measures in future to ensure that a backlog does not develop again. Relevant Government agencies, including the Department of the Treasury and the Office of Parliamentary Counsel, should have sufficient resources dedicated to implementing these measures.

We encourage the Government to pursue a model of an open, public legislative timeline. An open and transparent timeline for legislative change gives taxpayers a necessary level of certainty when it comes to dealing with that change.

It is crucial that any changes to Australia's tax system are analysed thoroughly and with due recognition of the potential regulatory and compliance impact on affected businesses and individual taxpayers. We note Treasury's critical role to ensure that tax law accurately reflects policy intent and implementation arrangements allow for efficient and effective revenue collection.

We also urge the Government to carefully consider options to complement the decrease of resources at the ATO such as supporting greater reliance on pre-filling and/or automation of the income tax return process for taxpayers with simple tax affairs.

Deregulation

The Tax Institute supports the Government's continued deregulation initiative and the publishing of a regulation impact statement in respect of each tax reform. Careful consideration should be given to how the success of this initiative will be measured. It is our view that this initiative should be clearly distinguished from the repeal of redundant provisions, with the focus being on genuine time and cost savings for users of the tax system.

Further, deregulation should not be at the expense of sound reform in areas such as regulation of financial advisers providing tax advice and reform of trust taxation discussed above. The deregulation initiative should not be used to avoid addressing these complex but necessary areas requiring tax reform.

Child care affordability

Studies show that, in economic terms, the labour supply behaviour of women with young children responds negatively to child care price. This means that, as the price of child care increases, there is a corresponding decrease in the number of hours that women are in paid employment. This indicates that, for parents who need to use child care to work, child care is a cost of employment. Despite the longer term benefits of returning to work (including making superannuation contributions), in the short term, the costs of child care significantly reduce the value of doing so.

The Henry Review found that the current system of child care assistance recognises that parents and children in different circumstances will require different amounts of assistance. It concluded that the amount of child care assistance should be higher at low income levels and means tested as income increases, but that a base level of assistance should be provided across the income spectrum to facilitate participation.

Under the current tax law, a tax deduction is in general restricted to amounts incurred in income-producing activities and is generally not available for a loss or outgoing of a private or domestic nature irrespective of whether that expenditure is necessarily incurred in order to earn income. Child care costs are deemed private expenditure not incurred in producing assessable income and thus not deductible, although they are, in most cases, essential because of a taxpayer's employment.

The Henry Review acknowledged that our current system is confusing, with high effective marginal tax rates adversely influencing taxpayer behaviour. Means-testing access to child care payments contributes to high effective marginal tax rates. It encourages lower income earners back into the work-force with the presumption that higher income earners will return to work irrespective of the concession.

Tax deductions for the costs of child care, if appropriately targeted, would encourage highly educated women who bear the primary responsibility for domestic duties to return to work. Tax deductions should only be available to reduce the tax on income from employment or self-conducted business income so that they are unequivocally tied to enhancing productivity. That is,

there is no point giving a subsidy to reduce the tax on investment income. As such, we do not support subsidising the child care expenses of a parent who is still at home earning bank interest or share dividends.

The advantage of making child care costs tax deductible is that it relies on market forces (rather than Government intervention) to determine work force participation and to allow legitimate costs of work force participation to be appropriately deducted from income. Tax deductibility would assist in eliminating existing positive incentives for primary carers to stay out of the workforce, yielding a variety of benefits for individual families as well as the nation.

Tax-deductibility of child care costs therefore deserves careful consideration and study. Women in lower marginal tax brackets cannot benefit as greatly from child care deductibility as women on higher marginal tax rates and hence some level of means-tested support may well be necessary. However, this assistance should be in addition to a wider consideration of deductibility of child care costs.

Many in the community would regard it as undesirable to make the tax system less progressive. A refundable tax credit or cash grant would avoid this outcome. Therefore, if the Government is not prepared to endorse tax deductibility it should consider making available a refundable tax credit or cash grant.

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