The Tax Institute

25 January 2024

The Hon Dr Jim Chalmers MP, Treasurer
The Hon Stephen Jones MP, Assistant Treasurer and Minister for Financial Services
C/- Budget Policy Division
Treasury
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Dear Treasurer and Assistant Treasurer,

Federal Budget 2024–25

The Tax Institute welcomes the opportunity to make a submission in response to the call by the Assistant Treasurer and Minister for Financial Services, the Hon Stephen Jones MP, on 1 December 2023 for such submissions regarding priorities for the Federal Budget 2024–25.

In the development of this submission, we have closely consulted with our National Technical Committees and broader membership to prepare a considered response that outlines the key issues related to the Australian tax, transfer and superannuation systems that we consider should be prioritised by the Government.

2023 was an uncertain year for the Australian people and economy. Since the pandemic, Australians have faced a series of persisting problems such as soaring inflation and the burden of rising living costs. During this time of uncertainty, several major changes to our tax and super system have been announced or introduced, often resulting in increased complexity and compliance costs for taxpayers. The challenges posed by the current unsustainable system are likely to grow in the future. As highlighted in the Intergenerational report 2023, Australia needs to manage and address the spending and societal pressures brought on by an ageing population and declining levels of economic growth and living standards for future generations.

Our current tax and superannuation systems are not suitable to support our people and economy during these future challenges. The current heavy reliance on inefficient taxes, particularly personal income tax, hinder the Government's ability to raise sufficient revenue to provide a better future for Australians. Further, the ever-increasing complexity of our tax and superannuation systems makes it increasingly difficult for taxpayers to voluntarily comply in a cost-effective manner. The Tax Institute is of the view that the Government should begin the process of implementing holistic reform of Australia's tax and superannuation systems, and re-design them with the core concepts of efficiency, simplicity, and fairness in mind. It is important to begin this process now, given that meaningful and lasting reform will take time to design and implement.

Further, within the existing tax system, there are several key areas which require the Government's attention, such as consideration of the concept of a 'worker' to replace the existing concepts of 'employee' and 'contractor', addressing the use of inefficient taxes such as the Fringe Benefits Tax (**FBT**) and luxury car tax (**LCT**), and simplification of superannuation caps, thresholds and concessions.

While holistic reform is progressed, we consider that there are a number of interim priorities that the Government should address. Importantly, the administration and overall integrity of our tax system face a risk due to a decline in student numbers studying accounting, law and related fields. Over a prolonged period, this will result in a shortage of needed skilled resources. This is a known issue and has been recognised by the Government by including tax accountants in the temporary skills shortage list.

We acknowledge that the persistent shortage of skilled resources in this field is not limited to Australia; it is a global problem that cannot be adequately addressed through migration alone, even when combined with technology. However, the complexity of our tax system further exacerbates these challenges. To overcome these issues, it is crucial to enhance the skills, knowledge, and tax literacy of all Australians. This can be achieved by improving funding structures within the government, streamlining dispute processes, increasing funding for tax clinics to support the most vulnerable Australians, and implementing better education programs about the importance and functioning of the tax system in schools nationwide.

In addition, the Government should provide certainty on the extensive and growing list of announced but unenacted measures (**ABUMs**) and outstanding Board of Taxation (**Board**) reviews. The Australian community needs certainty over their taxation obligations to enable them to make decisions that grow their businesses, support their livelihoods, and promote the health of the economy.

These steps are necessary to ensure that our tax and superannuation systems are better prepared for the upcoming future challenges.

Our detailed response is contained in **Appendix A**.

The Tax Institute is the leading forum for the tax community in Australia. We are committed to shaping the future of the tax profession and the continuous improvement of the tax system for the benefit of all. In this regard, The Tax Institute seeks to influence tax and revenue policy at the highest level with a view to achieving a better Australian tax system for all. Please refer to **Appendix B** for more information about The Tax Institute.

If you would like to discuss any of the above, please contact The Tax Institute's Senior Counsel – Tax & Legal, Julie Abdalla, on (02) 8223 0058.

Yours faithfully,

Scott Treatt
Chief Executive Officer

Todd Want
President

APPENDIX A

We have set out below our detailed comments and observations for your consideration.

Comprehensive review and reform of the Australian tax system

The Australian tax and superannuation landscape is complex and imposes an unduly costly compliance burden, requiring taxpayers to allocate a significant portion of their limited resources that could otherwise be spent on growing their businesses. The Tax Institute considers that these systems are overdue for comprehensive reform to become sustainable and efficient in the long term, and support Australia's economic growth.

As detailed in our Case for Change report, The Tax Institute recommends a rebalancing of Australia's tax mix as a key part of these reforms. Australia's primary source of tax revenue is personal income taxes. Its reliance on this source of revenue is notably higher than other countries forming part of the Organisation for Economic Co-Operation and Development (**OECD**[1]). To increase productivity and workforce participation, The Tax Institute is of the view that Australia should reduce its reliance on income tax and increase its use of more efficient broad-based taxes, such as goods and services tax (**GST**) and land taxes. The Government should also consider increasing the GST rate to better align with other OECD countries, while broadening the GST base to raise the revenue needed to support Australia's future needs through a simpler and more efficient system. We acknowledge that low and middle-income earners may be disproportionately impacted by such reforms. These taxpayers should be supported with lower income tax rates that reflect the extent of the disproportionate impact and more effective use of the transfer system. The Tax Institute also considers that a single, lower rate corporate tax rate, no higher than 25%, should apply to all companies irrespective of their aggregated turnover or proportion of passive income. This will help to make Australia a more attractive location for investment and support healthy competition in the Asia-Pacific region.

As part of the reform process, the Government should consider abolishing taxes which raise limited revenue but create disproportionately high compliance burdens for taxpayers and administrative costs for the ATO. Examples include the Fringe Benefits Tax (**FBT**) and the Luxury Car Tax (**LCT**). Some of these taxes, like the FBT, could be replaced with more streamlined and efficient regimes that better balance the compliance burden with the revenue raised.

[1] *Parliamentary Budget Office, Trends in personal income tax (Budget Bite, 18 November 2022), Retrieved from: https://www.pbo.gov.au/sites/default/files/2023-01/Budget%20Bite%20-%20Trends%20in%20personal%20income%20tax.pdf*

It is important that the reform process commences promptly. Meaningful and holistic reform will take time to accomplish, as it involves mapping out the trajectory and implementing it gradually over an extended period. It is crucial for the reform process to be thoroughly considered and appropriately implemented.

Respond to Board of Taxation reviews

The Board of Taxation has undertaken a number of reviews to which the Government has not yet responded. The Tax Institute is of the view that the Government should respond to and commence detailed and meaningful consultation on the implementation of key proposals contained in these Reviews, including the:

- Review of the tax treatment of digital assets and transactions in Australia
- Review of capital gains tax (CGT) rollovers
- Report introducing an asset merger rollover relief
- Review of the income tax treatment of certain forms of deferred consideration.

This will provide certainty for taxpayers and assist them to comply with their taxation obligations. Consultation is important to ensure that future legislative developments in light of these Reviews are carefully designed to target systemic issues, future-proofed, and avoid compounding compliance costs for taxpayers.

Announced but unenacted tax measures

The Tax Institute is of the view that the Government should address the significant number of ABUMs that have remained unenacted for a lengthy period. Our Incoming Government Brief: June 2022 sets out most of the ABUMs that relate to the tax and superannuation systems, and prioritises the outstanding measures based on thorough analysis against key objectives. While progress has been made to address many of those ABUMs, a significant number remain unenacted. It is imperative that the Government indicates how it wishes to progress with the outstanding ABUMs.

Below are some longstanding ABUMs that, in our view, should be progressed as a priority.

Corporate tax residency

The current corporate tax residency rules contain significant complexity and uncertainty, creating difficulties for taxpayers and potentially disincentivising international companies looking to expand their operations into Australia. Although the ATO recently updated its guidance on the application of the central management and control test[2], technical amendments to the law are still required.

[2] *Australian Taxation Office, Central management, and control test of residency: identifying where a company's central management and control is located (PCG 2018/9, 1 November 2023)*

As detailed in our Federal Budget 2023-24 submission (**2023–24 submission**), we consider that the Government should:

- implement the Board of Taxation's recommended changes to the corporate tax residency requirements[3] whereby companies incorporated offshore will be treated as an Australian resident for tax purposes if they have a 'significant economic connection to Australia'; and
- adopt the previous Government's announcement that it would consult on broadening the amendments to the corporate tax residency rules to trusts and corporate limited partnerships to promote greater consistency in the law and simplify the tax compliance process for international groups with multiple types of entities.

Division 7A reform

Division 7A of Part III of the *Income Tax Assessment Act 1936* (**ITAA 1936**) is an anti-avoidance measure that impacts many private companies and privately held groups. Significant uncertainty remains around the application of Division 7A, with numerous amendments being implemented since its introduction in 1997. The constantly changing environment has led to increasing amounts of confusion and compliance costs for taxpayers.

As part of the Federal Budget 2016–17, the previous Government announced proposed changes to the Division 7A rules to improve their integrity and operation based on the recommendations from the Board of Taxation's 2014 Report.[4] These proposed amendments have been deferred multiple times, leaving taxpayers in a prolonged state of uncertainty about their taxation obligations.

The Tax Institute is of the view that the Government should progress with the proposed amendments after engaging in sufficient and meaningful consultation with key stakeholders in the profession. This will allow for a consolidation of ideas and ensure that the changes are still appropriate in light of notable developments that have been made since 2017. It will also allow time to ensure that any changes strike the right balance between compliance costs, complexity, and the need for integrity.

Superannuation

As detailed in our Case for Change document, Australia's superannuation system is in need of comprehensive review and reform to ensure it can continue to support self-sufficient retirement and reduce the financial burden of an ageing population.

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[3] *Commonwealth of Australia (2020), 'Review of Corporate Tax Residency: A report to the Treasurer', Retrieved from: https://taxboard.gov.au/sites/taxboard.gov.au/files/2020-10/Signed%20-%20Final%20report%20-%20Review%20of%20Corporate%20Tax%20Residency.pdf*

[4] *Commonwealth of Australia (2014), 'Post Implementation Review of Division 7A of Part III of the Income Tax Assessment Act 1936: A report to the Treasurer', Retrieved from: https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2015/07/Division7a_Report.pdf*

Below, we have briefly outlined key issues that should be prioritised. Further detail can be found in our 2023-24 submission .

Superannuation thresholds and indexation

The complex overlay of caps, thresholds and concessions in the superannuation system causes taxpayers to inadvertently breach the rules and face severe consequences. The Tax Institute considers that the superannuation caps, thresholds, and concessionary measures should be reformed to be more consistent and simpler.

Further, The Tax Institute is of the view that the Government should abolish proportionate indexation of the transfer balance cap (**TBC**). Current indexation methods may create separate TBC for an individual that is different to the rest of the population, making it difficult for taxpayers to understand and meet their obligations, and for the ATO to administer the regime. Instead, indexation should apply universally to all superannuation fund members so that there is greater certainty about members' TBC amount and to free up the ATO's compliance resources from this area.

Capital gains rollover for product rationalisation

The Tax Institute considers that the Government should consult on introducing a capital gains tax (**CGT**) rollover for superannuation funds where products are rationalised and streamlined within the same fund. This would enable superannuation fund members to switch to different products within the same fund as alternative products become available without triggering adverse CGT consequences. Such a change would help to ensure that our superannuation system is agile, keeps up with changes in consumer preferences, and can better support superannuants in their retirement.

Short-term access to superannuation for downsizers

As outlined in our Federal Budget 2022-23 submission, The Tax Institute is of the view that the Government should allow retirees to temporarily access their superannuation funds to help retirees downsize their homes without financial obstacles, subject to appropriate integrity measures. This would also encourage movement in the housing market which is under increasingly immense pressure.

Introduce an all-encompassing concept of a ‘worker’

In light of the renewed focus on the meaning of ‘employee’ following two High Court cases[5] in 2022, and the recent passing of the Fair Work Legislation Amendment (Closing Loopholes) Act 2023, The Tax Institute considers this an opportune time to re-examine the definition of ‘employee’ across the tax and superannuation landscapes. A harmonised definition across Federal and State or Territory Acts can reduce the existing complexity, promote certainty for taxpayers, and lessen the compliance burden.

As detailed in our Federal Budget 2021-22 submission, the emergence of new work relationships, such as the sharing or ‘gig’ economy, has introduced further complexity to tax compliance in a dated system. The OECD has reported findings of growth across its member countries in the number of workers earning income outside of traditional employment arrangements. This change is driven by factors like demographic shifts, favourable taxation regimes, and labour market regulations.[6] Accordingly, The Tax Institute supports reform to ensure that our system is future-proofed and keeps up with these changes. We are also of the view that adopting a broad definition of a 'worker' that includes employees, contractors, and those in non-traditional work relationships, would simplify employment taxes (both at a State and Federal level) and aspects of the superannuation system, while reducing red tape and opportunities for businesses to exploit labour contracts.

Abolish and replace fringe benefits tax

FBT accounts for less than 1% of Australia’s net cash collections but imposes a disproportionately high compliance cost on businesses due to complexities in the archaic regime. The FBT tax gap is consistently one of the highest tax gaps, highlighting the inefficiency and complexity of the regime. For the 2020–21 income year, the estimated net FBT tax gap increased to 28.2% or $1.275 billion from net gap of 20.1% in 2019-20.

The Tax Institute continues to recommend that the existing FBT regime be abolished and replaced with a principled approach in line with recommendation 112 of the Henry Review. As detailed in our Case for Change, this would assist with consistent interpretation of the laws in alignment with sound policy objectives, and reduce red tape for employers in complying with their obligations.

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[5] *CFMMEU v Personnel Contracting Pty Ltd* [2022] HCA 1 and *ZG Operations Australia Pty Ltd v Jamsek* [2022] HCA 2

[6] *OECD (2020), “How Tax Systems Influence Choice of Employment Form”, in Taxing Wages 2020, OECD publishing, Paris*. Retrieved from: https://read.oecd-ilibrary.org/taxation/taxing-wages-2020_ea6d4837-en#page1

Increased Government funding for agencies and tax clinics

Permanent funding for the ATO

As highlighted in our 2023-24 submission, the ATO plays an integral role in the administration of Australia's taxation and superannuation systems. This covers a range of responsibilities from collecting revenue to taking responsibility for distributing and managing significant economic incentives. The ATO also provides technical and interpretive guidance to taxpayers and tax practitioners to assist them navigate the complexities and requirements of the law. This broad portfolio of responsibilities requires the ATO to be sufficiently funded to ensure that it can undertake its activities and fulfil its responsibilities and obligations in an expedient and efficient manner.

Feedback from our members indicates that the ATO is currently under-resourced in key areas, resulting in significant delays for taxpayers. This results in a lack of guidance for the community, delays in standard processing, requests for private rulings and responses to objections, and a backlog in unresolved disputes with the ATO. Historically, a significant portion of the ATO's funding has been provided for taskforces aimed at recovering monies or increasing tax collections from specific market segments.

The Tax Institute considers that this approach of allocating temporary and limited funding for specific compliance programs supports the ATO only in addressing a small category of high-risk behaviours through targeted compliance programs. We consider that the ATO and the broader community would be better served by increased and longer-term funding for other business areas within the ATO that develop interpretative guidance, resolve disputes, support taxpayers in meeting their taxation and superannuation obligations, and modernise underlying technologies that can assist taxpayers and tax practitioners better manage their tax affairs. The provision of greater funding to these business lines would ensure that ATO resources are being applied to assist a greater number of taxpayers to comply with their tax obligations. This would have the flow on effect of increasing voluntary compliance and revenue collection.

Additional funding for the Treasury

As outlined in our 2023-24 submission, increased funding to the Treasury must also be considered by the Government. Treasury plays a key role in analysing and addressing policy issues from a holistic economic perspective, understanding government and stakeholder circumstances, and responding rapidly to changing circumstances. The Treasury is significantly under resourced particularly in areas dealing with tax policy and law. An increase in funding will assist Treasury in addressing the long list of ABUMs, as well as other policy matters of greater and wider concern.

Additional funding for the National Tax Clinic program

The Government has acknowledged the need for additional funding for tax clinics and allocated funds for 5 new tax clinics in the Federal Budget 2023-24. While this is a positive step, we are of the view that more funding is necessary for the tax clinics. Currently, the ATO manages the funding and grants for the National Tax Clinic program on a clinic-by-clinic basis, but there is limited funding available for other important services like promoting the program externally. To support the increasing number of vulnerable taxpayers, it is crucial to allocate more funding to the National Tax Clinic program. This will enable the clinics to effectively promote themselves and meet the rapidly growing demand for their services. With increased funding, the tax clinics can expand their outreach initiatives and ensure that vulnerable taxpayers stay connected with the ATO and can meet their tax obligations. Additionally, the funding can be used to enhance collaboration and joint educational efforts among the existing clinics, improving their operational management.

Tax mechanisms to minimise impacts of climate change

The tax system can be used to encourage or deter certain behaviours to promote environmental sustainability and tackle the growing challenges posed by climate change. Although still before Parliament, The Tax Institute welcomes the small business energy incentive contained in Schedule 2 to the Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2023 which proposes to allow eligible businesses to temporarily claim an additional 20% deduction on spending that supports electrification and more efficient uses of energy. We consider that measures like this should be permanent features of our tax system.

However, The Tax Institute is of the view that further changes should be considered to incentivise the adoption of green energy. The Government should consider consulting on developing an environmental policy that encourages the use of sustainable technology, such as the following measures:

- creating a permanent bonus deduction or instant asset write-off for investments in ‘green’ technologies and energy efficiency. The small business energy incentive noted above is a step in the right direction although it only applies to the 2023–24 income year. Other measures could include, for example, accelerated depreciation for upgrading solar panels or investment that encourages the use of recycled water; and
- extending the current green (clean) building managed investment trust tax concession reducing the withholding tax rate from 30% to 10% for non-resident investors. This may help to encourage greater foreign investment in Australia.