TAX POLICY STATEMENT

STRONGER · FAIRER · SIMPLER

A tax plan for our future

© Commonwealth of Australia 2010

ISBN 978-0-642-74602-3

This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to the:

Commonwealth Copyright Administration
Attorney General's Department
3-5 National Circuit
BARTON ACT 2600

Or posted at:

http://www.ag.gov.au/cca

Internet:

This report and other related information is available at:

www.futuretax.gov.au

Printed by CanPrint Communications Pty Ltd

FOREWORD

Australia has many significant economic advantages that can provide the foundation for growth and prosperity well into the future, provided we get the policy settings right. Our substantial natural resources, strong growth in demand for our exports from countries in our neighbourhood, and the quality and resilience of our people as demonstrated most recently during the global financial crisis, give us cause for confidence that Australia's best days lie ahead.

We also know our natural advantages and the confidence we have in the future will not be enough on their own to guarantee growth and prosperity. The world is changing fast; our population is ageing; and the continued strength in our terms of trade brings the challenges posed by a two-speed economy where sectors benefiting from a mining boom attract resources from other industries. Only if we face up to such challenges, and keep up with the pace of economic change, can we expect to succeed in the post-crisis global economy.

The central vision of this tax plan is to invest Australia's minerals bounty in a stronger and broader economy for all our people. It seeks to ensure Australians get a fairer share of the coming boom and that the dividends of that boom are directed where they can make the greatest contribution to jobs and sustainable growth.

The plan outlined in the pages that follow will strengthen and broaden our economy at the same time as it starts down the path of a fairer and simpler tax system for Australian families and businesses. It recognises that in order to allow strong economic growth in every corner of the country, across all industries, businesses, and particularly smaller businesses, Australia must have a tax system that helps them thrive.

The Government's plan comprises a company tax rate cut for all companies beginning from the 2013-14 income year with a one year head start for small business, who will also have access to instant write-off of assets up to $5,000 and a single depreciation pool for most other assets. National savings will increase as result of increasing the superannuation guarantee to 12 per cent and other reforms to improve fairness in the superannuation system. The Government will also establish a new infrastructure fund to alleviate capacity constraints.

This tax reform plan will be funded by a new Resource Super Profits Tax commencing on 1 July 2012.

The initiatives outlined in this statement are ambitious on their own, but are still only a first step in a decade long process of reform. In the coming months and years, the Government will have more to say about improvements to the personal tax system to make it simpler and fairer. Like the reforms contained in these pages, any further changes will seek to convert our natural advantages and recent successes into enduring gains for all Australians.

CONTENTS

INTRODUCTION

The Government's tax reforms will build a stronger economy and a fairer, simpler tax system for Australian families and businesses.

The initiatives detailed in this statement represent a clear and compelling reform agenda. They are designed to maximise Australia's opportunities while also meeting the challenges posed by the ageing of our population and shifts in the global economy that will see the return of boom conditions in our mining sector.

These reforms will invest in sustainable economic growth and the jobs and higher wages that brings. One third of these investments will be in cuts to business taxes, particularly small business; another third in infrastructure and the resources sector; and another third to boost national savings through the superannuation accounts of millions of Australians.

Firstly, the Government is acutely aware that the resource boom means non-mining related sectors of the economy may grow less quickly. A strong Australian dollar means other exporters and import competing businesses face a more difficult economic environment. These businesses may find themselves in the 'slow lane' of a two-speed economy.

The Government is assisting these sectors by reducing the company income tax rate to 29 per cent for the 2013-14 income year and to 28 per cent from the 2014-15 income year. More investment means more capital, higher productivity and higher wages. While benefiting mining investment, this will also assist other industries, such as manufacturing and construction, to provide jobs and opportunities in other parts of the country. This will ensure that the benefits of reform are shared more widely throughout the country.

Small business will particularly benefit from a head start in cutting the company tax rate from the 2012-13 income year, a new instant write-off for assets worth up to $5,000 and simplified depreciation for most other assets. These measures will cut red tape for small business while also providing further tax relief.

Secondly, the resources sector will benefit from a number of measures, including a new infrastructure fund which will allow States to address bottlenecks inhibiting our resources getting to market.

A Resource Exploration Rebate will help exploration companies, particularly small companies, search for new deposits. Improved treatment of expenses under the Resources Super Profits Tax (RSPT), relative to royalties, will also assist entrepreneurial investment and resource exploration. The sector will benefit from renewed investment, growth and employment.

Thirdly, the tax reform package will improve national savings. A new superannuation contribution of up to $500 will be provided by the Government for workers with income up to $37,000. This will effectively return the tax on the superannuation guarantee contributions made to their fund for 3.5 million low income earners. Over 50s with low superannuation balances will also be given more generous contributions caps to allow them to make catch up contributions.

The Government will also gradually increase the superannuation guarantee to 12 per cent. Long lead times will allow businesses to plan and to benefit from the Government's tax reforms before making the first increased contribution of ¼ of a per cent in 2013-14.

These measures to improve national savings will assist in meeting the challenges of an ageing population. More Australians will be able to retire with the security of an adequate income. The reforms are also likely to result in more Australian assets being owned by Australians through their superannuation funds. Finally, these national savings measures will assist in keeping pressure off interest rates.

The Government will introduce a RSPT from 1 July 2012 at a rate of 40 per cent on super profits made from the exploitation of Australia's non-renewable resources. This will mean efficient and fair taxation of Australia's natural resources.

Refunding royalties as part of the RSPT and cutting the company income tax by 2 percentage points is expected to increase GDP by 0.7 per cent and real wages by 1.1 per cent in the long run. The infrastructure investments will also provide long lasting benefits to resource-rich States and the rest of the country. These reforms will address the challenges of managing the demands on a resource rich economy by expanding our economy's ability to increase production.

These structural changes to the tax system will make the Australian economy stronger as more tax revenue will come from immobile natural resources, and less from more mobile workers and capital. Our society will be fairer because fair prices will be charged by the Australian community for its non-renewable resources. The benefits of tax reform will be distributed widely; and people on lower incomes will be better able to achieve a secure retirement. Small businesses will also benefit from a simpler tax system and the Government will soon announce initiatives to make the system even simpler for families.

These reforms have been informed by extensive community consultation, expert advice and the findings of an independent review of taxation.

We will meet our future challenges in a fiscally responsible way and ensure that the Australian community receives a fair return for their non-renewable resources. These measures will be contingent on the successful implementation of the RSPT. They are a statement of our community values and aspirations. Most of all, they will help convert our recent economic success and the quality and resilience of our people into enduring gains for all Australians, their businesses, and our economy.

A TAX SYSTEM FOR A STRONGER ECONOMY

A BETTER TAX SYSTEM FOR A STRONGER ECONOMY

The Government's reform package will make the economy stronger.

The Government will reduce the company tax rate to 29 per cent for the 2013-14 income year and to 28 per cent from the 2014-15 income year. This will encourage investment in Australian companies, boosting the capital stock. Because workers will have more capital, they will be more productive and be paid higher wages.

The Government will also introduce a 40 per cent Resource Super Profits Tax (RSPT) on non-renewable resources from 1 July 2012. Under the RSPT, royalties will be creditable and refundable to projects. The RSPT taxes super profits, whereas royalties tax production. The RSPT therefore effectively removes the production and investment distortions of royalties from mining production.

Independent modelling by KPMG Econtech estimates the long run gain to GDP from these two reforms to be around 0.7 per cent. This increase in real GDP is broadly equivalent to $8½ billion in 2009 terms.

Average real after-tax wages (the after-tax wage rate adjusted for consumer prices) are projected to increase by around 1.1 per cent in the long run (equivalent to an extra $450 per year in the pocket of a worker on average weekly earnings). Changes to resources taxation and the cut in company tax rate are projected to lead to a long run increase in investment of around 2.1 per cent.

FISCALLY RESPONSIBLE TAX REFORM

The Government's tax reform agenda is fiscally responsible. This package is fully funded over the forward estimates and in the medium term. The reform agenda fully meets the Government's fiscal strategy, including the commitment to keep the tax to GDP ratio on average below the 2007-08 level of 23.6 per cent. And it strengthens the economy, generating a growth dividend that will be returned back to the budget to strengthen the fiscal position.

Table 1: Budgetary impact of the Government's tax reform agenda ($ million)[(a)]

	2010-11	2011-12	2012-13	2013-14
Company tax cut	-	-	-300	-2,000
Small business instant write-off and simplified depreciation	-	-	-	-1,030
Head start on a lower company tax rate for small business	-	-50	-300	-200
State Infrastructure Fund	-	-	-700	-735
Superannuation - Increasing the superannuation guarantee rate to 12 per cent	-	-	-	-240
Superannuation - Raising the superannuation guarantee age limit From 70 to 75	-	-	-	15
Superannuation - Low income earners government contribution	-	-	-	-830
Superannuation - Concessional contributions caps	-	-	-545	-785
Resource Exploration Rebate	-	-	-520	-600
Resource Super Profits Tax	-	-	3,000	9,000
Total	**-**	**-50**	**635**	**2,595**

(a) Australian Taxation Office administration costs will be reported in the 2010-11 Budget.

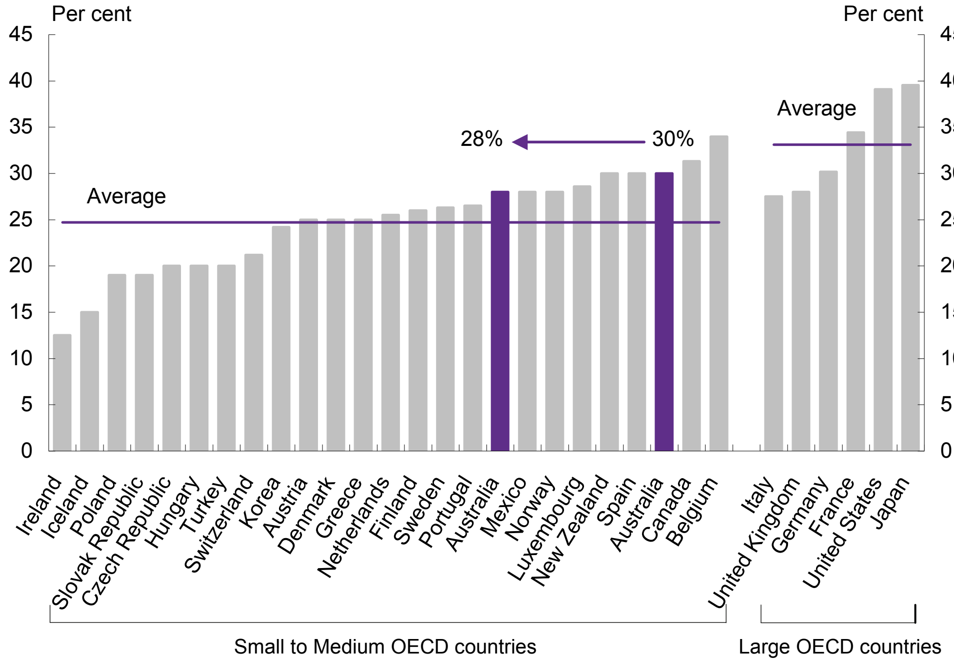
A LOWER COMPANY TAX RATE

The Government will cut the company tax rate to 29 per cent from the 2013-14 income year and then to 28 per cent from the 2014-15 income year. A lower company tax rate will improve incentives to invest in Australia. Increased investment in Australia will boost the capital stock available for Australians to work with. Greater capital intensity will lead to higher labour productivity and therefore higher real wages for Australian workers.

Emerging economies in our region will drive world economic growth over the coming decades. Australia needs to respond to remain an attractive place to invest and do business. Part of this response will be to ensure that the tax system supports investment and allocates resources to their most valued uses.

The Australia's Future Tax System Review found that Australia's company tax rate is high compared with other similar sized OECD countries. In 2009, Australia's 30 per cent company tax rate was around 5 percentage points higher than the average for small to medium sized OECD economies (Chart 1). In our region, economies such as Hong Kong, Singapore, Taiwan and Vietnam have much lower rates of company tax.

Chart 1: Statutory corporate tax rates, OECD countries 2009



Source: OECD Tax Database.

Reducing the company tax rate is expected to increase investment and therefore production across all sectors of the economy. The increase in production is likely to be greater for capital intensive sectors with high levels of incorporation, such as mining and construction.

Reducing the company tax rate will, in the long run, lead to an increase in real wages reflecting increased labour productivity as a result of capital deepening and increased demand for labour.

Reducing taxes on investment, particularly company income tax, will also encourage innovation and entrepreneurial activity. The Government's tax reform priorities will increase income for Australians by building a larger and more productive capital stock, and by generating technology and knowledge spillovers that boost the productivity of Australian businesses.

With the expected continued growth of China and India, and more efficient taxation of non-renewable resources, Australia will continue to attract investment into its resource sector. Cutting the company tax rate will also help other sectors attract investment.

A HEAD START FOR SMALL BUSINESS

While large resource companies are enjoying robust demand for the commodities they produce, some small businesses in Australia have not emerged from the global financial crisis in such good shape. To assist small business companies the Government has decided to provide them with an early start to the cut in the company tax rate.

This measure reduces the company tax rate to 28 per cent for eligible small business companies from the 2012-13 income year — one year earlier than the start of the general reduction in the company tax rate. This will have cash flow benefits for small business companies and enable them to reinvest more of their profits.

There are approximately 720,000 small business companies that can benefit from this measure. This measure will provide a direct benefit to small business companies that retain their profits and will provide an incentive for many more to do so. This will promote investment and help many small businesses to expand and grow.

INCREASING INVESTMENT IN INFRASTRUCTURE

Unless we have the right infrastructure, we will not be able to take full advantage of our current opportunities. Key capacity-building infrastructure like ports and roads are vital for our resources sector and also for all Australian industries and for Australian workers.

The introduction of the RSPT will enable the Government to make infrastructure spending a permanent structural feature of State and Commonwealth budgets for the first time.

The Government will establish a new infrastructure fund for the States worth $700 million in 2012-13, and that will grow over time. This fund will enable investments to be made in nation building infrastructure, including the infrastructure necessary to develop Australia's natural resource wealth.

The States will not have to wait until resource projects are complete and production comes on line for infrastructure funding to become available. The fund will enable States to deliver infrastructure as it is needed, including when new projects are being built, rather than having to wait to collect revenue until projects commence operation.

PROMOTING RESOURCE EXPLORATION

The Government will also deliver on its commitment to promote investment in exploration, through a new Resource Exploration Rebate.

Under the new rebate, companies will receive a refundable tax offset at the prevailing company tax rate for their exploration expenditure. The rebate will apply to the same range of exploration expenses as are immediately deductible under the existing tax law, provided the exploration is carried out in Australia.

As a further boost to the Government's support for renewable energy, expenditure incurred in exploring for geothermal energy will be eligible for the Resource Exploration Rebate.

The rebate is a simpler and more effective way to promote investment in exploration than a flow-through shares scheme.

It will provide significant cash flow benefits to small, pre-profit exploration companies. Compared with larger more diversified companies, these smaller companies face a competitive disadvantage because they have little taxable income against which to deduct their exploration expenditure. They have to wait until they earn taxable income before they can benefit from tax deductions. With the Resource Exploration Rebate they will receive an immediate cash benefit.

BETTER CHARGING FOR OUR NATURAL RESOURCES

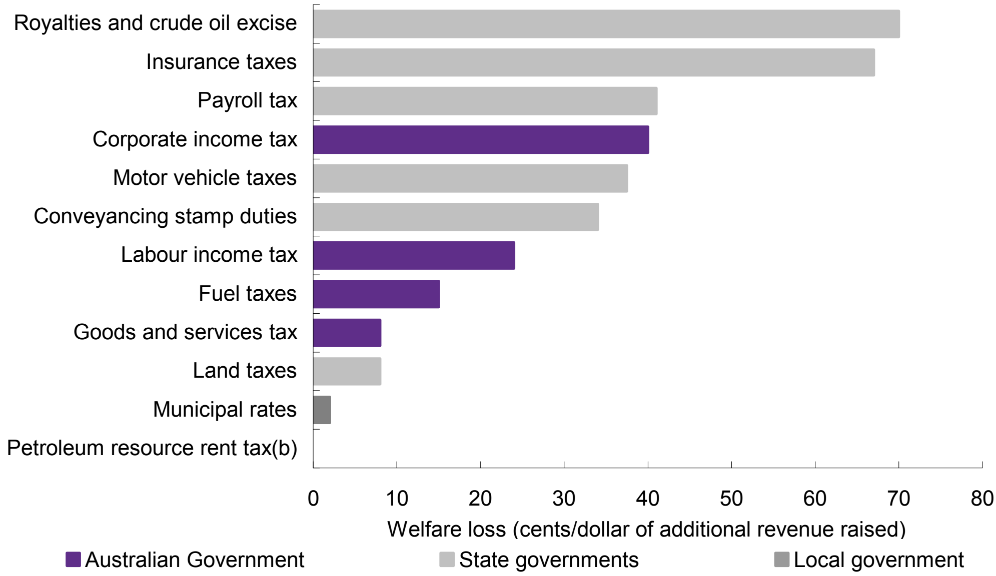
The RSPT is a more economically efficient arrangement for charging for our resources.

Royalties are amongst the most inefficient taxes levied in Australia (see Chart 2). An inefficient tax results in lower GDP because it induces people to change their work, investment or saving decisions.

States will continue to receive a stream of royalty revenues which will be relatively stable and will occur early in the life of a resource project. This will assist them to meet their fiscal objectives.

More detail on the design of the RSPT and the plan for consultation with industry is presented in *The Resource Super Profits Tax: a fair return to the nation*, available at www.futuretax.gov.au.

Chart 2: Marginal welfare loss from a small increase in selected taxes[(a)]



(a) The welfare effect of varying each tax has been assessed using the KPMG Econtech MM900 general equilibrium model of the Australian economy. The welfare loss is the loss in consumer welfare per dollar of revenue raised for a small (5 per cent) increase in each tax, simulated individually. It is measured as the amount of lump sum compensation required to restore the representative consumer's level of satisfaction to its original level, after returning the revenue raised by the tax to the consumer as a lump sum transfer. The extent of such compensation reflects the distorting effect of the tax on the economy.
(b) The petroleum resource rent tax is modelled as a pure rent tax giving rise to a zero welfare loss. In practice, a small increase in this tax could be expected to induce some welfare loss. However, it would be expected to rank as one of the more efficient taxes in the chart.
Source: KPMG Econtech, produced for the Review of Australia's Future Tax System (2009).

The RSPT provides a refundable credit for royalties paid by resources companies. This arrangement will remove many of the existing tax impediments to mining investment, but will allow States to continue to levy royalties. Resource projects that currently pay royalties but do not earn sufficient profits to be net payers of the RSPT will have an incentive to expand. Prospective projects that are expected to yield low resource profits will pay less under the RSPT than under royalties, and so the disincentive to invest in new or existing marginal projects will be removed.

In the long run, the RSPT will encourage greater investment and employment in the resources sector. When implemented, the RSPT will be one of the most efficient taxes levied by any government. As a tax on resource rents or super profits, the RSPT will have minimal effect on investment and production decisions.

Improving national savings and superannuation adequacy

The Government is introducing superannuation reforms that will deliver substantial improvements in retirement incomes for Australian workers, boost national savings, and help meet the challenges of an ageing population.

The Government will increase the superannuation guarantee (SG) rate from 9 to 12 per cent over time. The rate will be increased in small increments from 1 July 2013 to 1 July 2019, with increments of 0.25 percentage points on both 1 July 2013 and 2014, and subsequent annual increments of 0.5 percentage points per annum. This measure will not only increase the adequacy of retirement incomes for Australian workers over time, but also contribute to national savings. As detailed in the next section, other superannuation measures include raising the SG age limit from 70 to 75, a Government superannuation contribution for low income earners and help for older workers to make catch-up contributions.

Australia's system of compulsory superannuation savings, which has been in place since 1992, has contributed significantly to increasing national saving. The pool of superannuation assets under management in Australia today is over $1 trillion, increasing our investment potential and ensuring that our reliance on foreign funds is lower than otherwise.

The superannuation measures that the Government is introducing are projected to generate an additional $10 billion by 2020 and $35 billion by 2035 in private saving each year. In aggregate, the measures are projected to add around $500 billion to the existing pool of superannuation savings, and contribute to further increasing national savings by around 0.4 per cent of GDP by 2035.

A TAX SYSTEM THAT IS FAIRER

A FAIR SHARE OF AUSTRALIA'S NATURAL RESOURCE WEALTH

The RSPT is at the centre of the Government's tax reform agenda. This tax is designed to tax resource projects on the basis of profits rather than production, but also to ensure that Australia gets a fair return from our natural resource wealth.

Australia's abundant non-renewable resources can be expected to continue to command high prices, supported by demand from China and India in particular. Given the size and value of Australia's non-renewable resource stock and expected continued strength of commodity prices, it is important the community receive an appropriate return from the exploitation of their resources by private business.

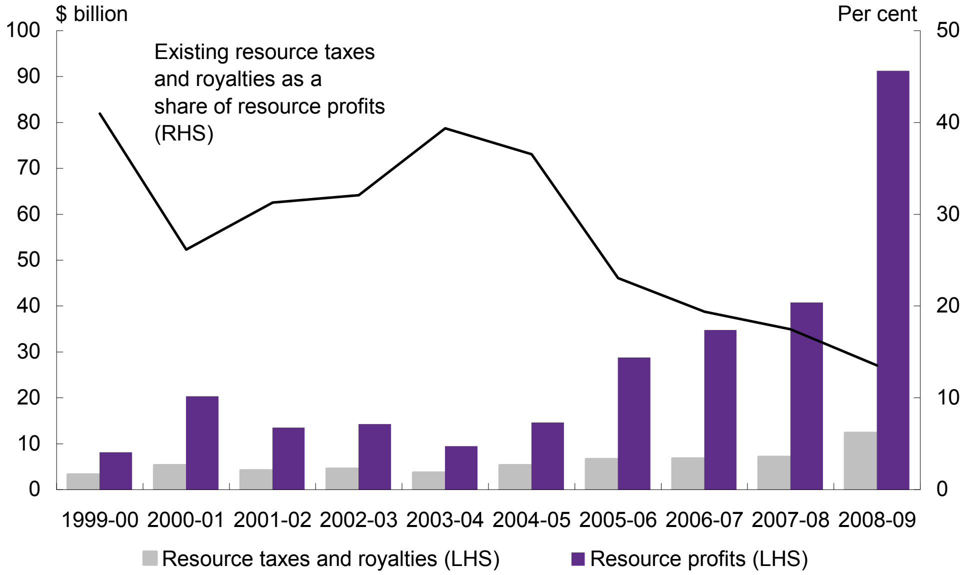
The current structure of taxes and charges on non-renewable resources does not serve the Australian community well.

The RSPT is a world class reform. It sets a new benchmark for resource taxation. Most of Australia's non-renewable resources have been made cheaply available for private commercial interests to make substantial profits, part of which is distributed through dividends to shareholders, including foreign shareholders.

Governments have allowed private firms to extract non-renewable resources in return for a charge, typically per unit of production or percentage of price, regardless of actual production costs. These charges have not kept pace with the increased value of Australia's resources.

The effective resource charge (charges as a percentage of super profits earned) has almost halved from an average of around 34 per cent over the first half of this decade to less than 14 per cent in 2008-09. Existing resource taxes and royalties have only captured a small share of the increased value of the nation's resource deposits. Resource profits were over $80 billion higher in 2008-09 than in 1999-00, but governments only collected an additional $9 billion through resource charges (see Chart 3).

Chart 3: Existing arrangements are inefficient and unresponsive



Note: Estimates of resource taxes and royalties exclude income taxes.
Source: Treasury estimates.

The RSPT will yield a return to the community as a share of resource profits that is more comparable to the early 2000s, before the last mining boom.

FAIRER SHARING OF MINING BOOM OPPORTUNITIES

As well as boosting profits, strong growth in the mining sector means relatively strong growth in particular regions and in wages. Many industries linked to mining, such as the construction industry or industries that provide goods and services to mining employees, are likely to benefit.

Higher incomes for Australians also lead to higher demand for goods and services right across the economy. For example, while the retail industry may feel pressure in competing with mining-related sectors for workers, it is also likely to benefit from greater sales.

However, the success of natural resource exports can create challenges for some sectors of the Australian economy.

One market mechanism for encouraging resources to flow to sectors producing higher valued outputs is the exchange rate. Strong demand for our natural resources can appreciate the exchange rate, making it harder for other exporters to compete overseas. This can also make it harder for domestically oriented producers to compete against imports. The capital and labour that would otherwise go into these sectors is therefore encouraged to move to the expanding sector.

Independent modelling by KPMG Econtech estimates that cutting the company tax rate to 28 per cent and introducing the RSPT combined with the removal of the impact of royalties will expand mining output by 6.6 per cent in the long run (considered by KPMG Econtech to be 5 to 10 years). All other industries are expected to expand by 0.3 per cent in the long run.

Reforming our resources taxation arrangements will primarily benefit the mining sector. The mining boom already means that additional workers and capital will be needed in the mining sector to increase production. This struggle of other export and import competing sectors to maintain output growth has become known as the two-speed economy. Overall, GDP is expected to increase by 0.3 per cent in the long run with the introduction of the RSPT and removal of the impact of royalties.

In contrast, reducing the company income tax rate to 28 per cent is likely to benefit all sectors of the economy, but particularly those that make use of significant private capital. Construction, mining and manufacturing are expected to have particularly large increases in output. The overall increase in long run GDP from cutting the company tax rate is expected to be 0.4 per cent.

The combined effect of introducing the RSPT, which effectively removes royalties and cutting the company tax rate by 2 percentage points, is a long run improvement to GDP of 0.7 per cent.

The Government's policy direction is to make the most of Australia's mineral resource wealth by reforming resource charging arrangements, allowing tax relief which redistributes the gains to other sectors. Rather than slowing the fast resource-driven lane of the two-speed economy, the policy aim is to reduce barriers limiting the growth of the slower lanes.

FAIRER CONCESSIONS FOR SUPERANNUATION

The Government supports the need for superannuation concessions to underpin adequate retirement incomes for Australians, now and in the future. The Government is also concerned about the low level of tax concessions afforded to the superannuation of lower income earners.

The Government will improve the fairness of the superannuation system by providing tax concessions for those Australians who most need assistance to save for retirement. 3.5 million Australians currently get next to no concession on their superannuation guarantee contributions or, worse, have these contributions taxed more heavily than their normal income, due to the tax on superannuation contributions. From 1 July 2012, a new superannuation contribution of up to $500 will be provided by the Government for workers with income up to $37,000. This will effectively return the tax on the superannuation guarantee contributions made to the funds of low income earners.

The Government also recognises that many workers want to make catch-up superannuation contributions as they approach retirement. From 1 July 2012, the Government will allow individuals aged 50 and over with total superannuation balances below $500,000 to make up to $50,000 in concessional superannuation contributions. This doubles the cap of $25,000 which is scheduled to apply from 1 July 2012. This measure will improve the equity of the existing superannuation system by targeting concessions towards those with the greatest need to build their retirement savings.

From 1 July 2013, the Government will also extend the superannuation guarantee to workers who are aged between 70 and 75, to ensure they are remunerated on the same basis as their younger co-workers.

Fairer concessions for superannuation will help lower income earners save and older workers catch up on their retirement savings.

A TAX AND TRANSFER SYSTEM THAT PROVIDES THE RIGHT INCENTIVES AND REWARDS EFFORT

The Government understands the importance of having a fair tax system — one that does not stifle opportunity, that allows effort to be rewarded and also ensures that no Australian falls behind. The Government has made some significant changes in recent years to increase the fairness of our tax and transfer system.

By delivering permanent increases in pension payments the Government has strengthened the financial security of Australia's age, carer, disability and service pensioners.

The Paid Parental Leave scheme for primary carers, to be introduced from 1 January 2011, is an important step towards ensuring arrangements support families when they need it most. Over time it will also increase workforce participation, particularly for women.

The Government sees tax reform as a decade-long process. The initiatives outlined in this statement are ambitious on their own, but they are still only a first step. In the coming months and years, the Government will have more to say about improvements to the personal tax system to make it simpler and fairer. It will promote informed and sustained policy debate across the whole of the tax system. Like the reforms contained in these pages, they will seek to convert our natural advantages and recent successes into enduring gains for all Australians.

A TAX SYSTEM THAT IS SIMPLER

A simpler tax and transfer system means people have to spend less time complying with their tax obligations and working out their transfer entitlements. Time spent interacting with the tax and transfer system is a 'deadweight cost' on society. In particular, time and resources wasted on tax compliance and administration could be better spent in other ways.

These costs are ultimately built into the prices of goods and services sold in the community, making us all worse off. Since there are often economies of scale in meeting tax obligations, smaller businesses tend to bear a higher proportion of the burden.

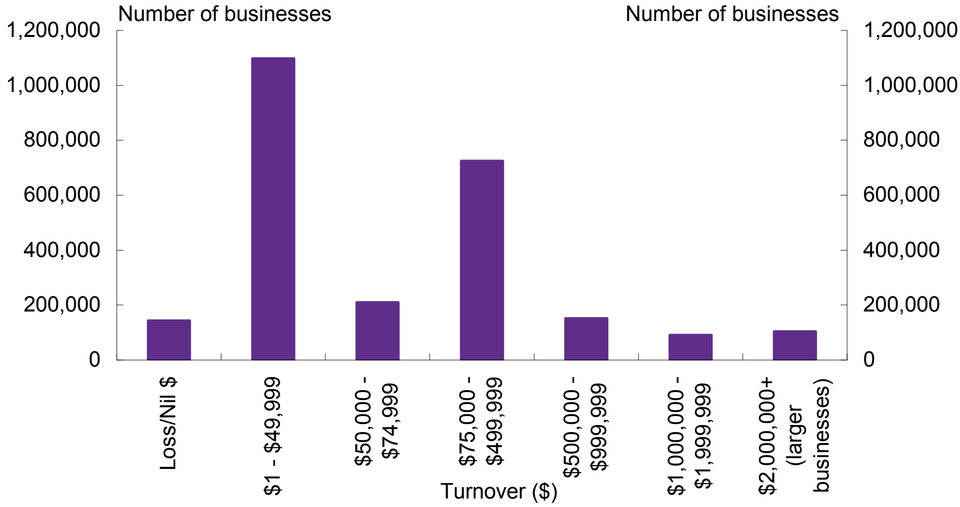
Some complexity in the tax and transfer system is unavoidable. The community often has goals for the tax and transfer system other than raising revenue as efficiently as possible, including operating a fair system. However, some types of complexity can be both unfair and inefficient. For example, those with access to innovative tax advice can claim more deductions than those with limited means. Complexity such as this has no place in a modern tax system.

Australia's tax system is also complex because of the number of taxes levied by many different levels of government. Further, some jurisdictions have the same taxes but they are often administered in different ways, creating unnecessary uncertainty and additional costs for business.

SIMPLER TAXES FOR SMALL BUSINESS

The Government's small business tax package recognises that the vast majority of businesses operating in Australia are small businesses (a business with a turnover of under $2 million). This is illustrated in Chart 4 below.

Chart 4: Businesses by turnover (2007-08) ($)



Source: Treasury estimates based on Australian Taxation Office data.

These businesses are more likely to be held back by red tape and complexity than larger businesses. The small business tax package will build on a range of existing taxation measures that are designed to reduce the complexity facing small businesses in their interaction with the tax system.

From the 2012-13 income year, the threshold for a low value asset which can be deducted immediately will increase to $5,000. This will enable small businesses to write off immediately many of their assets, significantly reducing their need to track assets for depreciation purposes. In addition, small businesses will be able to allocate all other depreciable assets (except buildings) to a single depreciation pool, which can be written off at a generous 30 per cent rate. This will remove the need for small businesses to monitor two different depreciation pools and will further simplify their tax affairs.

In addition to reducing the compliance costs faced by small businesses, these changes will boost their cash-flow at a time when they are investing for growth.

Along with the early cut to the company tax rate for small business companies, these measures constitute a substantial package of support for Australia's small businesses.

SIMPLER TAXES FOR WORKING AUSTRALIANS

The tax system could be made simpler for working Australians. Many everyday Australians find the personal tax system complex, and the overwhelming majority seek professional assistance to complete their annual tax returns.

The Government is interested in exploring ways to reduce the burdens the tax system places on working Australians, while maintaining their access to the appropriate tax treatment of legitimate expenses.

The Government will have more to say on this issue in coming months.

SIMPLIFYING THE CLIENT EXPERIENCE OF THE TAX AND TRANSFER SYSTEM

It is also important to move towards a system that improves how Australians interact with the tax and transfer system. People find their interactions with the tax and transfer system to be complex and fragmented. The Government is interested in looking at how the tax and transfer system should operate into the future in a way that helps people and businesses make informed decisions that are in their best interests.

These reform opportunities will be considered as part of the Government developing a single overarching strategy for service delivery reform.

A LONG-TERM REFORM AGENDA

The Government recognises how large a task it is to reform Australia's tax and transfer system.

The existing system is the product of hundreds of individual policy changes made over many decades. Very few of these have reduced complexity in the system. Even those changes that, when taken in isolation, appear to benefit the nation as a whole, can often have interactions with other aspects of the tax system that are hard for policymakers to predict and to therefore take into account.

Such a complex system makes tax reform a difficult process. It is, however, a very important one for Australia's economic future. Some studies have estimated the costs of taxpayers *complying* with their taxation obligations to be in the order of 1 to 2 per cent of GDP. That is, 1 to 2 per cent of the value of everything produced in Australia in any one year is spent by taxpayers on simply ensuring that they pay the right amount of tax.

Compliance costs are an ongoing cost, borne every year. If we were able to reduce this cost by one third, even using the more conservative estimates we would succeed in releasing around $4 billion every year. This could be spent on more productive activities. The Government is determined to ensure that the dividend from making a simpler and more efficient tax system is realised, to the benefit of all Australians.

As set out under *A tax system that is simpler* above, the Government is considering further changes in the areas of personal income tax that will make the system simpler and lower compliance costs for taxpayers. Announcements in these areas will be made in the coming months.

If re-elected to a second term, the Government will continue to foster informed and sustained public debate on tax reform in consultation with the community.

MEASURE DESCRIPTIONS

RESOURCE SUPER PROFITS TAX

A RSPT will commence on 1 July 2012 at a rate of 40 per cent on profits made from the exploitation of Australia's non-renewable resources.

The RSPT will replace the crude oil excise, and operate in parallel with State and Territory royalty regimes.

The Australian Government will provide resource entities with a refundable credit for state royalties paid. The refundable credit will be available at least up to the amount of royalties imposed at the time of announcement, including scheduled increases and appropriate indexation factors. Refunding royalties allows the States to continue to collect a stable stream of revenue from royalties, while removing the effects they have on investment and production.

To provide certainty for projects already covered by the Petroleum Resource Rent Tax (PRRT) the Government will consult with industry on arrangements that would allow an irrevocable election into the RSPT. That is, projects within the scope of the PRRT will remain in the PRRT unless they elect to transfer into the RSPT. The government anticipates that, over time, many projects within the scope of PRRT will migrate into the RSPT.

The Australian Government will consult extensively with stakeholders on technical design issues during the period before the scheme commences. This process will start with an initial round of consultations over coming weeks that will focus on how to finalise transitional arrangements for existing projects and other key elements of the architecture of the tax.

The Government will undertake consultation on the detailed design of the RSPT. More detail on the design of the RSPT is presented in *The Resource Super Profits Tax: a fair return to the nation*, available at www.futuretax.gov.au.

STATE INFRASTRUCTURE FUND

World class infrastructure is essential to ensure Australia continues to be an attractive place to set up a business, creating new jobs for now and the future. The Australian Government will use some of the proceeds from the RSPT to support States in providing such infrastructure.

This fund will help States invest in infrastructure to support improved living standards.

Investing in major infrastructure will help improve our potential to grow the economy into the future. Key capacity-building infrastructure like ports and roads are vital for all Australian industries, and for Australian workers.

The Government will start this fund from 2012-13 so that it delivers resources to the States when they are needed — as projects are built. The States will not have to wait until resource projects are complete and production comes on line for infrastructure resourcing to flow.

The total amount of the infrastructure fund will start at $700 million in 2012-13 and will grow over time.

Resource exploration rebate

The Government will provide a refundable tax offset at the company level, set at the prevailing company tax rate, for exploration expenditure (provided the exploration is carried out in Australia).

The Resource Exploration Rebate is a simpler and more effective means of fulfilling the Government's election commitment to support the development of Australia's resource sector.

It will be available for exploration expenditure incurred on or after 1 July 2011. As part of this measure, the definition of exploration expenditure will be expanded to include expenditure incurred in exploring for geothermal energy.

In comparison to the existing deductions for exploration expenditure, a refundable tax offset provides a stronger incentive to carry out exploration.

Payment of a refund under the Resource Exploration Rebate would ordinarily lead to a franking debit in a company's franking account. If a company's franking account is in deficit at the end of an income year, the entity is liable to pay franking deficit tax. This would have the effect of immediately clawing back the benefit of the Resource Exploration Rebate for small companies that are in tax loss. To prevent this outcome, if a company receives a refund of the Resource Exploration Rebate, a franking debit will not arise in the company's franking account. However, when the company subsequently pays a pay as you go (PAYG) instalment or income tax, a franking credit will not arise until the deferred franking debits are recovered.

Expenditure incurred in exploring or prospecting for minerals, petroleum or quarry minerals can be immediately deducted, subject to the taxpayer passing certain tests. Expenditure on depreciating assets that are first used for exploration can also be written off immediately.

For companies with little or no taxable income, the existing deductions simply add to tax losses that are carried forward and offset against future income. This timing difference erodes the net present value of the tax deduction, and in some cases the loss may not be able to be used.

Around 4,300 companies in the resources sector stand to benefit from the new refundable tax offset.

Including exploration for geothermal energy is important given Geoscience Australia's preliminary analysis that suggests Australia's potential geothermal energy is roughly 1.2 billion petajoules (equivalent to 20,000 years of Australia's primary energy use in 2005).

The measure will commence on 1 July 2011. The Government will consult on the exposure draft legislation to give effect to the rebate.

CUTTING THE COMPANY TAX RATE

The company income tax rate will be reduced to 29 per cent for the 2013-14 income year and to 28 per cent from the 2014-15 income year, in conjunction with introducing the RSPT on 1 July 2012.

This will move Australia towards achieving an internationally competitive tax rate. It will make Australia a more attractive place to invest.

Reducing the company tax rate to 28 per cent, funded through the introduction of the RSPT is expected to increase long run GDP by 0.4 per cent.

The reduction in the company tax rate will lead to higher economic growth and wages. Introducing the RSPT at the same time will ensure that the community receives a more appropriate return for extraction of its non-renewable resources.

The current company tax rate is higher than the rate in other comparably sized OECD countries.

Company income tax rates have fallen across the OECD over the past 30 years. The fall in the average statutory corporate tax rate across the OECD has been fairly continuous.

Australia has, until recently, followed this trend, with the company income tax rate falling from 49 per cent in the mid-1980s to its current rate of 30 per cent in 2000-01.

Income taxes on investment, such as company income tax, can lead to lower domestic productivity by increasing the required pre-tax return for an investment (the cost of capital) and reducing the incentives to invest. This can result in a smaller domestic capital stock, which leads to lower productivity and lower wages.

EARLY CUT IN THE COMPANY TAX RATE FOR SMALL BUSINESS

The Government will reduce the company tax rate to 28 per cent for eligible small business companies from the 2012-13 income year. This will:

- increase the cash flow of eligible small business companies; and
- enable these companies to reinvest more of their profits back into the company to expand and grow their businesses.

The measure provides direct and practical benefits to many small businesses. There are approximately 720,000 small business companies that can benefit from this measure.

The Government will consult on the implementation details of this measure before preparing exposure draft legislation. Relevant issues for consultation include instalment and franking arrangements.

SMALL BUSINESS INSTANT ASSET WRITE-OFF

The Government will enhance and expand the existing capital allowance concessions available for small businesses from the 2012-13 income year by:

- allowing small businesses to immediately write-off assets valued at under $5,000 (this is up from $1,000 under the present law); and
- allowing small businesses to write-off other assets (except buildings) in a single depreciation pool at a rate of 30 per cent. Currently, small businesses can allocate assets to two different depreciation pools.

Enhancing the existing depreciation concessions provides a simple and effective mechanism for assisting small businesses. Increasing the immediate write-off threshold to $5,000 will enable small businesses to immediately deduct the costs of a significant proportion of the assets that they purchase. This will:

- increase their cash-flow by deferring their tax liabilities (that is, they pay less now);
- reduce compliance costs by removing the requirement to calculate depreciation allowances and track assets for depreciation; and
- make asset ownership more attractive than leasing or debt financing.

Removing the long-life pool and allowing small businesses to depreciate assets (other than buildings) in a single pool further simplifies the depreciation calculations.

The measure provides a direct and practical benefit to up to 2.4 million small businesses.

This measure will commence from the 2012-13 income year. The Government will consult on the details of the changes in 2010-11.

INCREASING THE SUPERANNUATION GUARANTEE RATE TO 12 PER CENT

This measure will increase the superannuation guarantee (SG) rate from 9 to 12 per cent, with increments of 0.25 percentage points in the first two years, and 0.5 percentage points thereafter. The increase will be phased in from 1 July 2013 to 1 July 2019, as shown in the following table.

Table 2: Superannuation Guarantee increases

Year	Rate (%)
2013-14	9.25
2014-15	9.5
2015-16	10
2016-17	10.5
2017-18	11
2018-19	11.5
2019-20	12

A major challenge is to ensure an adequate retirement income for our ageing population. The *2010 Intergenerational Report* underlines the challenges faced from our ageing population. The number of Australians aged over 65 is projected to grow from 3 million to 8.1 million by 2050. Over the next 40 years, the ratio of working age Australians to those aged over 65 will decrease from 5-to-1 to just 2.7-to-1.

The measure directly addresses issues raised by our ageing population, and boosts private and national savings, bringing broader benefits to the community and nation.

- It will significantly increase the future retirement incomes for many Australian workers, improving the adequacy of those retirement incomes. It seeks to strike the right balance, allowing people to have enough income to enjoy both their working life and retirement.

- The measure builds on measures to strengthen the Age Pension which were announced in the *2009-10 Budget*.

The measure has a three-year lead time, with increases in the SG rate not beginning until 1 July 2013. This will allow employers time to adjust to the new levels. While employers will take increases in SG contributions into account when negotiating future wage agreements, wage increases are expected to be sufficient to ensure that, overall, real wages continue to grow.

RAISING THE SUPERANNUATION GUARANTEE AGE LIMIT FROM 70 TO 75

This measure will raise the SG age limit from 70 to 75, with effect from 1 July 2013.

- Workers aged 70 to 74 will be eligible to have SG contributions made on their behalf for the first time.
- The new SG age limit will now match the age limit for voluntary and self-employed contributions.

Around 33,000 employees are expected to benefit from this measure, which will improve the adequacy and equity of the SG system.

Currently, the SG only applies to people aged up to 70. In contrast, employers can make voluntary deductible superannuation contributions for employees under 75, and self-employed people can make deductible contributions until they turn 75. Individuals aged from 70 to 74 are less likely to be able to negotiate voluntary superannuation contributions with their employers.

Increasing the SG age limit will provide an incentive for mature workers to remain in the workforce. The 1 July 2013 start date allows most employers time to negotiate future wage settlements in the light of the change.

GOVERNMENT SUPERANNUATION CONTRIBUTION FOR LOW INCOME EARNERS

This measure will provide a superannuation contribution of up to $500 annually for low income earners, with effect from 1 July 2012.

Currently all concessional superannuation contributions are taxable in the fund at a flat rate of 15 per cent. As a result, low-income earners receive little or no concession. This measure will improve the fairness of superannuation taxation arrangements by effectively returning the tax payable on superannuation guarantee contributions made for low-income earners.

The amount payable under this measure will be calculated by applying a 15 per cent matching rate to the concessional contributions made by or for individuals on adjusted taxable incomes of up to $37,000, with an annual maximum amount payable of $500 (not indexed). The amount will be paid into a superannuation fund of an individual to directly boost their retirement savings.

Concessional superannuation contributions made from 1 July 2012 will be eligible with the first Government contribution paid in 2013-14. The Government will consult on the details of the changes.

HELPING OLDER WORKERS MAKE CATCH-UP CONTRIBUTIONS

From 1 July 2012, the Government will allow individuals aged 50 and over with total superannuation balances below $500,000 to make up to $50,000 in concessional superannuation contributions. This doubles the cap of $25,000 which is scheduled to apply from 1 July 2012.

This will allow these individuals to 'catch up' on their superannuation contributions when they are most able. It will particularly benefit those who have had periods outside the workforce. The measure will improve the equity of the existing superannuation system by targeting concessions towards those with the greatest need to build their retirement savings.

The Government will consult with the superannuation industry on the operation of the $500,000 threshold.

As a result of these measures to ensure superannuation is stronger and fairer:

- a 30 year old earning average full-time wages will have an additional $108,000 in retirement savings[1];
- by 2020, an additional $10 billion per year in private saving will be available for investment into the Australian economy, including into nation-building infrastructure; and
- Australia's total superannuation savings are projected to increase by $500 billion by 2035.

1 Assuming full-time wages with SG.

Modelling

The likely long run macroeconomic impacts from the introduction of a RSPT including the removal of the impact of royalties and cuts in the company tax rate were modelled by KPMG Econtech using the MM900 model.

KPMG Econtech MM900 model

The KPMG Econtech MM900 model is a Computable General Equilibrium (CGE) model of the Australian economy that has been developed by KPMG Econtech.

The model has a high level of tax detail, which enables a broad range of the existing Australian taxes and policy changes to be modelled. These include company tax, resource royalties and resource rent tax. The ability to model resource rent tax relies on the identification in the model of 'economic rent' on fixed factors, such as land and resources, for some industries (including mining). The value of economic rent has been estimated by KPMG Econtech.

MM900 is a long-run equilibrium model. This means that the model converges to a long run, sustainable equilibrium, where the government Budget balances and a sustainable external balance are maintained. Model simulation results reflect these key model assumptions.

While the model provides a sophisticated means of assessing the impacts of policy change, MM900, like other models of this kind, has limitations. Some of these are discussed in the AFTS Report (page 75). Simulation results are sensitive to choices of parameters in the model, the model closure, as well as other assumptions with respect to economic behaviour of households and firms.

A more detailed overview of the MM900 model is provided in KPMG Econtech (2009) (available at www.taxreview.treasury.gov.au).The Australian Treasury provided the Government's policy parameters for tax reform to Econtech KPMG who then independently modelled their economic effects. KPMG Econtech were not involved in the policy development, while the modelling was independent of Treasury.

Results

The key macroeconomic modelling results are reported below.

Table 3: Long run macroeconomic impact of the reform package

Indicator	Impact (% change compared to baseline)
GDP	0.7
Investment	2.1
Employment	0.1
Wages (real)	1.1

Source: KPMG Econtech simulations using MM900 model

Specific qualifications to the modelling results

The simulation results reflect the structure of the base data for the model. This is based on 2004-05 input-output data (the latest available data with sufficient detail for the model), which has been up-rated by KPMG Econtech to 2009-10.

Results from CGE modelling should be seen as providing the general direction and a rough order of magnitude of the likely impact of policy shocks to the economy.

The modelling assumes that marginal investors are foreigners; that is, all additional investment is funded from overseas.

It should be noted that the modelled analysis is sensitive to assumptions used, particularly the degree of capital mobility. However, differing assumptions would only affect the size of the efficiency gains and not their direction. In the long run, the assumption of perfect capital mobility is plausible as used in the KPMG Econtech modelling in this statement.

The main economic impact of this reform package comes from the reduction in the company tax rate and abolition of existing resource charges and taxes.