

26th March 1999

The Secretary
Review of Business Taxation
Department of the Treasury
Parks Place
CANBERRA ACT 2600

Sir,

The Federal Chamber of Automotive Industries representing vehicle manufacturers and importers in Australia is pleased to respond to some of the matters raised in the review of business taxation “a platform for consultation”.

We are very concerned that there appears to have been no study of the likely industry impact of such changes.

In our initial submission dated 23 December 1998 (submission No 46), we identified possible problems with the application of Fringe Benefits Tax (FBT) as it relates to motor vehicles. Since the introduction of FBT in 1985, the take from motor vehicles has grown steadily and in 1998 represented 50% of all FBT collections. Under the present arrangements the FBT payable on a \$32,000 car travelling 20,000 per year is over \$6,000 pa. Thus over a four year period, the FBT at \$24,000 represents 75% of the tax inclusive price of the vehicle.

The proposals in Chapter 38 of discussion paper 2 Vol II would increase the FBT payable by up to 50%, or over \$9,000 pa. Thus over a four year lease, the FBT would exceed the taxed up value of the vehicle when new.

The Australian vehicle market is, by world standards, open, in that the level of protection is low. As a result, over 50% of new passenger cars are imported. The remaining less than 50% are locally produced, however, some 70% of locally built passenger cars are sold to fleets and Governments where FBT is paid on the vehicle. The effect of an increase in FBT will, therefore, have the greatest impact on locally built vehicles.

The present statutory formula was designed to tax, as best as possible, the private use of vehicles, hence the reducing rate as annual distance covered is increased. The Government of the day was mindful of the fact that business vehicles do travel greater distances than private vehicles, and the FBT scale reflects this.

Chapter 38 of the discussion paper also addresses the possibility of exempting certain entertaining from FBT. On a revenue neutral basis, any loss in FBT from entertaining would be offset by a higher level of FBT on motor vehicles. The Federal Chamber cannot condone a proposal where by certain entertainment is FBT exempt at the expense of motor vehicles.

As stated in the discussion paper the various options addressed “for reforming the statutory formula could have varying effects on the composition and size of the market. In general, where significant venue increases are likely to arise the market might see a decline in the growth of new car numbers.” Increasing the statutory formula as proposed would raise another \$400 million pa. This would cause a significant fall in new car sales, particularly locally produced vehicles.

The key suggestion in the RBT discussion paper rests on the FBT being payable by the employee, at the employee’s marginal tax rate. However, the Federal Treasurer has already rejected the transfer of FBT liability from the employer to the employee. On this basis, the proposed increase in FBT rates (to be offset where appropriate by a lower income tax rate) is no longer valid.

Rather, the Treasurer’s statement re-inforces the Chamber’s original position that the FBT rate be lowered to 40%, more closely align with the marginal tax rates expected after 1 July 2000.

Accelerated Depreciation

The RBT's objective was to find an acceptable solution to lowering the business (corporate) tax rate to 30%. This is an admirable objective fully supported by the Federal Chamber. However, we can not accept that an offset to the lower corporate tax rate would be the removal of accelerated depreciation.

The motor vehicle manufacturing industry is a highly capital intensive industry, with significant investment in new tooling, robotics and manufacturing plant and equipment.

This high level of investment, is related to model cycles and is therefore concentrated in short periods leading up to new model launch.

Accelerated depreciation allows the vehicle manufactures to improve their cash flows during these periods of high investment. Any move to restrict or remove accelerated depreciation would have a negative impact on vehicle manufactures at the time of greatest investment in Australia.

Investment by the four manufacturers in their passenger motor vehicle manufacturing activities rose strongly in the four years to 1997, and even higher levels of investment are forecast of the four year to 2001 (see 'State of the Australian Automotive Industry 1997', page 40). Total investment in the period 1994-97 exceeded \$2.2 Billion, and is expected to grow to \$2.7 Billion for the period 1998-2001.

These high levels of investment, which have also led to high levels of growth in automotive exports could be jeopardised should accelerated depreciation be removed.

Deferred Company Tax (DCT)

The suggestion that the present dividend imputation system is unnecessarily complex is not, in our view, accurate. The system has worked well for the past 13 years, and the regulations governing dividend imputation are not unduly complex. On the other hand, a deferred company tax system as proposed in the discussion paper will add complexity as it builds on the present system. Further, DCT will impose an additional tax at the entity level, thereby reducing Retained Earnings and Shareholder Net Worth.

The assertion that “countries operating foreign tax credit systems should allow credit for deferred company tax” has no foundation. The question of whether the DCT is a "tax on income" and therefore creditable has not yet been formally addressed nor canvassed with Revenue authorities of other jurisdictions with whom Australia has a Double Tax Treaty. DCT could therefore result in double taxation.

Of paramount importance in this matter that Australia is a net importer of capital, which is essential for our future development. A deferred company tax system, as proposed, would not encourage overseas investment.

Depreciation Limit

As advised in our submission of 23 December 1998, we are of the view that the depreciation limit on motor vehicles has not been relevant since the Fringe Benefits tax introduced in 1985. Retention of the depreciation limit results in double taxation on luxury motor vehicles. In a climate of taxation reform, the depreciation limit on motor vehicles should now be removed.

We are mindful of the amount of effort the RBT team has put into the discussion paper, and in general applaud the findings. However, as an industry, we cannot support:

- Increases in the rate of FBT applying to motor vehicles,
- the removal of accelerated depreciation, and
- the introduction of a deferred company tax.

Yours sincerely,

TERRY PENNINGTON
Executive Officer