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Mr John Ralph
Chairman
Business Taxation Review
Treasury

Dear Mr Ralph

18.5% Company Tax Rate with Assets Tax

I remain convinced that the subject of business taxation is so closely intertwined with personal taxation, and that personal taxation is so closely intertwined with welfare, that continuing to separate these into different entities and reviewing them independently offers nothing but short term fixes. Crisis management has the same feel.

The whole interaction between government, individuals and business needs to be examined for any solutions to be built on firm foundation.

The attached paper is a rewritten summary of a 1992 paper that I wrote. It produces a cohesive system that is integrated, transparent, simple and, I believe, logical and real. The system defined has an 18.5% Company Tax rate. This benefit to companies is offset by an Assets Tax that raises an amount equivalent to that raised by Consumption Taxes.

Since 1992 I have been attempting to get The System as a whole defined and rebuilt on solid foundations. The system I defined is, to me, the simplest, most fully defined and most just that I could conceive. There may be other options that are as defined and that are as easy to comprehend. I believe that any such systems will need to start from scratch and to qualify and quantify what base the system is built from and what benefits are provided to our society's people.

An offshoot of my work in this area has been the development of a computer program, TaxLink, that shows the total effect of government programs on individuals and families. I enclose a copy of this program for your information.

TaxLink allows detailed examination of the personal tax and welfare systems. It permits taxation and welfare rates to be adjusted. It includes adjusted rate records for the situation after the government's tax reform package is implemented. The results produced demonstrate that the Tax Reform Package is only a minor fix to a system that needs a cohesive, extensive review and overhaul. Another review of the size of this reform package will be needed within another 10 years because this one has not gone to the heart of the matter. Your review will become embroiled in this need unless your recommendations reflect the workings of The System as whole.

I hope that you will give this submission due consideration.

Thank you for your time

Glenn Thorpe

Our Social System

My basic beliefs are very simple. While our social scientists go on about progressive and regressive systems and the like I believe simply in simplification as a starting point.

We all interact financially with our government, and it is the nett effect of this interaction that matters. Until this nett effect is quantified we cannot hope to have any reasonable debate or analysis of the subject.

When identifying the nett effect of our interactions it becomes apparent that welfare payments and tax liabilities are one and the same thing. A reduction in taxation is equivalent to a welfare payment. Indeed Basic Parenting Allowance can be directly equated to the Dependent Spouse Rebate, and the Family Tax Payment can be directly equated to the Family Tax Rebate.

The two payments (or tax reductions) mentioned above are fully quantified and qualified. You can say the Dependent Spouse Rebate for a spouse with children is $1692, and you can say why the advantage is provided. The major tax reduction advantage however is the progressive tax scale; the low tax rates paid by all adults on income below $20,700 pa. This advantage is not quantifiable or qualifyable in its current form.

Any discussion on equity must consider this advantage provided by low tax rates; it must be quantified and qualified; how much is it, why do provide it, what does it represent.

So how much could it be? If we have a standard tax rate we can say how much the advantage is. With a standard tax rate set as below, the advantage provided is the amount shown

Tax Rate	Tax payable on $20,700 at tax rate	Tax actually payable	Advantage provided
25%	$5,175	$3,060	$2,115
30%	$6,210	$3,060	$3,150
35%	$7,245	$3,060	$4,185
40%	$8,280	$3,060	$5,220

I started this table at a 25% tax rate because this is the minimum tax realistically feasible to provide the basic services that society provides.

As you can see, considerable advantage is provided to every adult in the country. If it is not provided through this low tax rate it is provided through welfare.

So what does this advantage represent? Realistically we can categorize this advantage as a combination of four things, namely:

- Provision of a tax-free area for the unclaimable costs incurred in earning the money;

- Provision of some costs for the marginal cost of support of the person in an existing household, which directly equates to Family Payment, the Dependent Spouse Rebate and Parenting Allowance;
- Provision of some costs towards the infrastructure costs of providing a household; or
- Provision of luxury.

It is not politically viable for any politicians to admit to providing advantage for luxury, so qualifying what the payment represents must be a combination of the first three items.

Without considering who should get these advantages, let us try to put some sort of value on them.

A cost of $3,000 pa. is realistically a maximum amount that would be acceptable as unclaimable work expenses. This $60 pw. covers public transport travel costs and some other minor costs. At this level, if the standard tax rate is 30%, $900 of the advantage represents this.

Family Payment is paid as a fully analyzed payment for the marginal cost of support of a child in an existing household. It has been based on a calculated "poverty line" for many years and has been indexed to meet this "poverty line". The adult advantage of Parenting Allowance was based on the Dependent Spouse Rebate, which had not been indexed for many years prior to Parenting Allowance's introduction. Family Payment is $2,600 pa.

If the advantage represents household infrastructure costs we have a problem. Why is it provided to every adult, when these infrastructure costs are basically the same for a household no matter how many adults live in it. Shouldn't the advantage only be provided once per household?

If we therefore accept that the household infrastructure costs are the domain of welfare, we can say that if we have a tax rate that gives advantage of $3,500 pa. we are providing adults with their marginal cost of support and some benefit for their unclaimable costs associated with earning their income. The standard tax rate required to specify this as the advantage provided is 35%, very close to what the "normal" tax rate for working adults is.

Unfortunately, under any interpretation, this gives us a very major problem. The marginal cost of support we provide to children reduces very steeply as a person's income increases, whereas the same benefit provided to the adults doesn't start reducing until they start paying over 35% tax, and then it only reduces very slowly.

If we treat the reduction in this advantage the same for children as for adults we have to examine what it will cost, what sort of tax rate is need to treat the payments the same. Unfortunately we end up with three very ugly choices.

- If we have a tax rate of 25% all advantage is reduced at 100% of after tax money
- If we have a tax rate of 32% - 33% we can reduce the advantage at 50% of after tax money
- We require a tax rate of over 40% to provide the advantage to everyone irrespective of income.

As I said, they are all ugly.

Families with children are currently hit with the first option, nearly a dollar for dollar reduction. For every dollar they earn over a fairly wide range of income they see basically not one cent of it, YET THEY PAY 35% TAX, NOT THE 25% THEY SHOULD PAY.

Adults on the other hand are treated like the third option, their advantage is not reduced at all for a long time, and then it only reduces slowly, AND THEY ONLY HAVE A STANDARD TAX RATE OF 35% INSTEAD OF OVER 40%.

The tax rates quoted above are flat. If we include a tax premium to take high-income earners up to the same tax as they currently pay we can reduce the 40% tax rate required to provide the advantage to all irrespective of their income. We can also reduce the tax rate further by imposing restrictions on who can claim the Cost of work advantage. Why should people who have no costs because they either claim all their costs already (the self employed) or because they are provided with un-taxed allowances by their employers be permitted to claim this advantage?

These two changes bring the tax rate down to the 36% that we currently pay as standard. It is an equitable arrangement, all people are provided with the marginal cost of support.

Further substantial cost reductions from the childcare system (Childcare Assistance and Childcare Rebate), are possible if the childcare advantage is reduced for higher income earning families. It is envisaged that these changes would place a family currently receiving childcare advantage on a financial footing equivalent to where they are at the moment. These cost calculations are beyond my personal capabilities, which is one reason why this summary has not been updated from 1991 figures.

For adults this system parallels our current arrangements with relatively minor adjustments. This view though, with its quantification and qualification, provides an extremely solid base from which to critically examine advantage provided through the welfare and taxation systems. Without this solid base it is basically impossible to provide any meaningful analysis.

Part II - Accepting The Base

If the base outlined in the previous part is accepted the following, often unpalatable, statements are relevant.

- We can basically state as a maxim that "From this base, nobody, but nobody ever, ever, gets more advantage than a poor person"
- We have an extremely firm base from which to critically examine welfare and taxation.
- The real tax rate required to fund government expenditure and the advantage given is around 44% of the total income earned by the population. This comprises 36.5% in income taxes and 7.5% in consumption and other taxes.
- As advantage provided through the tax system is currently provided, and is not included in National Accounts as expenditure, this same treatment could continue. The basic advantage provided, of the marginal cost of support and unclaimable Cost of Work expenses, could go in the Accounts as a rebate or tax reduction where a person pays tax. It would only show as welfare expenditure where a person pays less tax than the advantage they and their family receive. Tax collections as a proportion of the income earned by the population (and GDP) would then be less than what they currently are.
- The base meets Mutual Obligation theory. If a person doesn't want to be a part of society, society still imposes its laws on that person. If the person drops out and starts to Hunt/Gather he is a thief. Compensation of food, which is basically what the marginal cost of support is, is compensation for society's imposition

Part III - Welfare

Accepting the base outlined allows us to critically examine welfare.

Care for the Aged - The first thing that hits one when one has a look at the aged is the advantage provided through superannuation contributions.

In 1991, a person contributing 9% of average male earnings to Superannuation for 40 years would receive a pay-out of some $200,000. Of this some $57,000 is advantage from the 20% reduction in the tax rate from 36% to 15%.

The captialized value of the average Age Pension in 1991 dollars was some $62,000 over the base.

This contradicts our maxim in a substantial way. If "From this base, nobody, but nobody ever, ever, gets more advantage than a poor person" is proper then the person who has paid this superannuation would not ever get very much Age Pension.

The unemployed, including Single Parents - from the base a single adult unemployed person's welfare becomes equivalent to one days work per week plus one weeks work every 12 weeks. For a married couple it becomes, combined, two days work a week plus 1 weeks work every 12 weeks. At these levels of work Work-For-The-Dole becomes more like subsidized employment, and is a viable alternative to paying benefits outright.

For youth the benefit provided over the base is minimal. Work-For-The-Dole at award rates would be for only a couple of hours each week.

Welfare highlights a number of distortions outstanding.

- Entitlement to Rent Assistance still has to be determined
- There is still some taxation advantage needed for Pensioners and low-income earners.
- $200,000 is not an excessive amount in superannuation, yet from the defined base this just about excludes any Age Pension entitlement.

These factors indicate the base, while good for analysis of the current system, still does not meet our society's standards or needs

Part IV - The Tax System

The problems with the welfare system indicates to me that we have too much reliance on income taxes. We only collect taxes on two of the three bases that are available, Income and Expenditure, while we exclude Assets. The 'Tax Premium" is essentially an additional tax on the wealthy in any case, but in this form it adds an unbalance to the system. An assets tax, collected at a rate that raises as much revenue as Consumption taxes, balances the system and goes a long way to solving the remaining welfare issues.

Of the 44% tax on income required to fund the system, setting 20% to be raised from each of Consumption and Assets Taxes, and 60% to be raised from Income Taxes provides a balanced system.

If the Assets Tax is raised on all assets that any entity controls we end up with a system very close to:

- A flat 27% Income Tax on individuals
- A flat 18.5% Company Income Tax
- A 12% Consumption Tax
- An assets tax of approximately 0.4% pa. on all entities controlling assets.

This pays for an increase in welfare to cover paying Rent Assistance to all Pensioners. Home owners then must pay an Assets Tax, which for low asset value houses will make these pensioners better off, for very high asset value houses it may make them worse off. Assets valued at around $400,000 are the breakeven point.

The Company Tax Rate is lower because an amount equivalent to an 8.5% income tax (20% of tax revenue) will be payable as Assets Tax twice, once by the company entity and once by the final person entity that owns the company stock. This means that profitable use of assets makes the entity better off, non-profitable use of assets requires an on going 0.4% tax each year.

An example -

A Company is valued by the market at $1 billion. It is 50% geared giving it control of assets worth $1.5 billion. The company returns 8% pa. on its value, or $80 million. This company currently pays 36% of $80 million or $28.8 million in Company Tax. If this is fully franked a shareholder paying standard tax doesn't pay anything more.

Under my proposal taxes paid would be:

- 18.5% tax on profits, or $14.8 million in Company Income Tax;
- 0.4% of $1.5 billion, or $6 million, in Company Assets Tax;
- 0.4% of $1 billion, or $4 million in Personal Assets Tax;

giving $24.8 million total tax revenue.

By permitting entities that control non-income producing assets to not pay any tax we are encouraging bad management, under-utilization of our country's resources and increasing the burden on those entities that do make a profit.

An 18.5% Tax Rate on profits would encourage low and medium capital value companies (as compared to their profits) to make their income in Australia rather than overseas.

We discourage useless investment; money parked in profitless ventures will still be subject to some tax.

Isn't this what we want for our country?