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

Dear Sir

Review of Business Taxation
"A Platform for Consultation"

I am pleased to provide for your consideration Australia Post's submission in response to the Review of Business Taxation, Second Discussion Paper - *"A Platform for Consultation"*

Australia Post was established in 1975 out of the Postmaster-General's Department and is the largest organisation providing mail, courier and parcel services within Australia. In 1989, Australia Post was corporatised and now operates as a statutory corporation under the Australian Postal Corporation Act 1989. The corporation is liable for all Local, State and Federal taxes.

The core business activities of the corporation are domestic and international letter and parcel services, retail agency business and financial services.

Australia Post earns almost half its revenue and more than two-thirds of its profit in fully competitive markets - delivering parcels (greater than 250g (8.8 oz)), newspapers, magazines, catalogues and providing financial services. After 1 July 2000, over 88% of Australia Post's business will be subject to competition.

Almost 36,000 Australians are employed by Australia Post at over 1500 sites with a further 3000 licensed sites across Australia comprising one of the largest integrated business networks in Australia.

The corporation is a world leader in postal technology and is currently committed to expending $600 million on upgrading the letters handling network by the installation of state of the art mail sorting machines.

Australia Post has a keen interest in the outcome of the Review of Business Taxation - and Tax Reform generally and is pleased to contribute to this important consultation process.

Yours Faithfully

Peter F. Dimech
Group Manager - Taxation

Australia Post

Submission to the Review of Business Taxation

Prepared in conjunction with
PricewaterhouseCoopers

Executive summary

Australia Post supports generally and welcomes the initiatives presented in the Discussion Paper *A Platform for Consultation* (“Report”) released by the Review of Business Taxation in February 1999.

As part of the consultation process, Australia Post submits this paper which, in part addresses, Australia Post’s concerns with particular measures contained in the Report. The following issues are addressed:

- Consolidation of corporate groups;
- Corporate tax rate;
- Fringe Benefits tax;
- Tax Write-off;
- Taxation of Company Distributions; and
- Research & Development Tax Concession.

Should further clarification be required on any of the measures addressed in this paper please contact:

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Consolidation of corporate groups

Can groups or entities switch in and out of consolidation?

The Report indicates that once a group elects to consolidate it would not be able to revoke its election subsequently. There is no reasoning provided in the Report to suggest why the election should be irrevocable.

Further the Report suggests the repeal of current grouping provisions. Effectively, companies are forced to consolidate and there will be no flexibility for specific concessions. Companies wishing not to transfer certain losses so as to pay extra tax to allow the franking of dividends will not be able to do so.

Recommendation

Australia Post believes that for many corporate groups, consolidation will not be optional.

The need to offset tax profits and losses and to implement tax efficient and efficacious corporate restructures would leave corporates no choice but to consolidate. The separate entity treatment for non-consolidated groups would, however, enable more flexibility.

Australia Post believes that this will limit many corporate decisions with respect to loss transfers, the management of franking credits and foreign tax credit positions. Flexibility with regard to franking and corporate restructures will be hindered under a consolidation regime.

It therefore follows that the election to consolidate should not be irrevocable. The Report provides no reason for making the election to consolidate irrevocable.

It is submitted that there may be valid commercial reasons why a group company member may elect to deconsolidate. A prospective acquisition of a consolidated group member may be less attractive as that company is jointly and severally liable for the group's tax debts.

Further, a group member that has temporarily gone into losses may also wish to deconsolidate if the consolidated group wants to maintain the existing level of tax payments to generate franking credits to enable it to pay fully franked dividends.

For the above reasons, Australia Post recommends that the election to consolidate be revocable subject to any necessary reservations to protect the tax revenue base. It is reasonable to assume that some constraints may be imposed (for example a two year holding period once an election has been made) to safeguard against annual switching.

Corporate tax rate

Australia's corporate tax rate of 36% is amongst the highest in the developed world. Without reduction in this rate, the Review's objectives of achieving internationally competitive and economically efficient business tax arrangements cannot be achieved.

Recommendation

Australia Post strongly supports the reduction in corporate tax rate to 30%.

Furthermore, it is Australia Post's views that the reduction in the corporate tax rate can be achieved without a large number of trade-offs.

Australia Post recognises that the reduction in corporate tax rate is required in order for Australia to achieve an internationally competitive tax system.

Australia Post does not believe accelerated depreciation should be removed in its entirety in order to generate sufficient revenue savings to fund the alternative measure of reduction in the corporate tax rate. Instead, it is recommended that the accelerated depreciation regime be retained at lower applicable depreciation rates enhanced by a concentration of the various bands.

The proposed trade-off to abolish the accelerated depreciation regime would impose significant costs on corporates such as Australia Post that would negate the benefits of a lower tax rate.

Fringe Benefits Tax

Alignment of FBT and income tax years

Alignment of the FBT and income tax years is considered to be an unfavourable result by Australia Post.

The current arrangement permits a three-month window in which FBT requirements can be satisfied prior to year-end and the commencement of the group certificate and corporate income tax compliance obligations.

This is particularly highlighted by the recent changes to require fringe benefits to be disclosed on group certificates. Regardless of the degree of automation it is unlikely that totally accurate calculations of fringe benefits can be achieved within the time frame allowed for producing group certificates at year-end.

This difficulty is of real concern for large employers such as Australia Post that currently has almost 37,000 employees at over 1,500 locations throughout Australia.

Amend the taxing of cars

The proposed changes to remove the concessional nature of the current statutory formula also raise major concern.

The increase in the statutory rates and the associated increase in tax payable on these benefits will have a considerable negative impact on many employees and therefore impact on future salary packaging.

Recommendation

Australia Post discourages any alignment of the FBT and income tax years on the basis that such alignment would place undue pressure with respect to its corporate income tax and group certificate compliance obligations.

Australia Post also discourages any increase in vehicle FBT rates in light of the significant GST disruption expected to used and new car values and the increased compliance costs that will be borne by Australia Post in the event of any increase in rates.

Tax Write-off

Accelerated depreciation

Accelerated depreciation enables a timing benefit in bringing forward the allowance of deductions for the decline in the value of an asset. The impact of the trade-off between maintaining accelerated depreciation and other capital allowance benefits with a reduction in the company tax rate is considerable.

In the event a consistent approach to write-off allowances is adopted, the option to apply effective life depreciation with a loading is preferred. This option would allow a more uniform treatment of wasting assets with differing effective lives by determining the rate of depreciation based on expected effective life of the asset increased by a fixed percentage loading.

<u>Buildings</u>

Including buildings and structures into a consistent regime with other depreciable assets is advantageous. Ultimately buildings do depreciate and therefore they should be incorporated into the general depreciation regime rather than a specific regime that governs building write-off.

The nature of buildings has changed and in many cases construction at greenfields industrial sites are tailored for specific specialised functions. With the advent of such buildings, there is a greater correlation and nexus between the term of the building life and the integrated equipment that is housed within the structure. Such buildings should clearly benefit from a standardised deduction regime.

Blackhole expenditure

“Blackhole” expenditures refer to the range of expenditures that do not currently qualify for deduction or for write-off but which should qualify.

These are mainly expenditures that are of a capital nature but for which there has been no specific legislative approach prescribed that would allow for tax deductions.

This mismatch results from the absence of specific provisions comparable with section 8-1 that would otherwise enable tax deductions for such capital costs.

Australia Post recommends that, in relation to “blackhole expenditure”, an equivalent provision to section 8-1 be enacted that prescribes, say 10 years, to write-off capital “blackhole expenditure” for tax purposes.

<u>Feasibility studies</u>

Australia Post supports the write-off of blackhole expenditure along the lines of Table 1.1 contained in the Report.

An approach consistent with the accounting regime for treatment of expenditure incurred in feasibility studies is required whereby a “catch all” capital allowance provision is created which seeks to capture expenditure not otherwise deductible under the general provisions.

Recommendation

As stated above Australia Post does not endorse the full abolition of accelerated depreciation as a trade-off to fund the reduction in the corporate tax rate but does accept a scaling back of the acceleration.

More specifically, in the event that buildings and structures were brought into the general depreciation regime, transitional arrangements applying only to new buildings and structures is appealing from a practical perspective.

Australia Post supports the enactment of a specific statutory provision that will enable “blackhole expenses” to be claimed as allowable deductions over a period of time. This would result in a more equitable and consistent outcome that accords with the general deduction provisions.

Taxation of Company Distributions

The proposal to impose a deferred company tax (DCT) on all dividends paid out of untaxed profits would create distortions through the reduction in reported after-tax profits for those companies required to pay DCT. Further, there is potential exposure to double taxation arising due to temporary timing differences.

The suggestion in the Report of a resident withholding tax would be preferred as a more attractive alternative in overcoming distortions whilst meeting the Government's objectives of taxing distributions at source.

Recommendation

Australia Post supports maintaining the existing rules for company taxation. However, the proposal for a resident dividend withholding tax is more supportable than the deferred company tax proposal as outlined in the Report.

Research & Development Tax Concession

The 150% R&D tax concession from 1985 to 1996 encouraged considerable R&D in Australia. The existing 125% rate is considered beneficial but does not attract or stimulate the amount of R&D activity that was promoted by the erstwhile 150% rate.

Recommendation

Australia Post recommends that the R&D tax concession be maintained and the effective rate raised to 150% to encourage and reward Australian R&D activity.

Australia Post is a leader in postal technology through the use of technological solutions to mail handling. In an environment of deregulation it is necessary that this use of technology is accelerated.

Post will obtain technology from Australian sources where these are available however frequently the core technology is necessarily imported. Restoring the R&D tax concession to 150% is likely to encourage Australia Post to increase its technological development locally and to source enhancements to the internationally available technology needs locally.