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SENATE

SELECT COMMITTEE ON A NEW TAX SYSTEM

Reference: A new tax system

TUESDAY, 2 FEBRUARY 1999

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SENATE

SELECT COMMITTEE ON A NEW TAX SYSTEM

Tuesday, 2 February 1999

Members: Senator Cook *(Chair)*, Senator Ferguson *(Deputy Chair)*, Senators Conroy, Gibson, Murray, O'Chee and Sherry

Participating members: Senators Brown, Colston, Harradine and Margetts

Senators in attendance: Senators G. Campbell, Cook, Conroy, Ferguson, Gibson, Harradine, Murray, O'Chee and Sherry

Terms of reference for the inquiry:

(1) That a select committee, to be known as the Select Committee on a New Tax System, be established to inquire into and report, on or before 18 February 1999, on the economic theories, assumptions, calculations, projections, estimates and modelling which underpinned the Government's proposals for taxation reform, contained in *Tax reform: not a new tax, a new tax system*.

(2) That, in conducting its inquiry, the committee examine the following matters:

(a) the estimated levels of revenue to be generated or foregone due to the proposed changes, including the estimated level of revenue to be generated by imposing a goods and services tax (GST) on the basic necessities of life (such as food, clothing, shelter and essential services) and books;

(b) the effects of the proposed changes on:

(i) national Gross Domestic Product,
(ii) national export performance and national debt,
(iii) the national Consumer Price Index, and
(iv) the distribution of wealth in the Australian community;

(c) the effects of the package on future federal budget revenues, expenditures and surpluses, including a critical assessment of the economic assumptions underpinning the Treasury's projections in this regard;

(d) the effects of the taxation and compensation package on disposable income and household spending power for a range of 'cameo profiles', including but not limited to those presented in the proposals, under the following scenarios:

(i) a GST extended to the necessities of life (such as food, clothing, shelter and essential services), and

(ii) a GST not extended to the necessities of life (such as food, clothing, shelter and essential services);

(e) with the aim of identifying families and groups who may be disadvantaged by the Government's proposals, focusing on lower and fixed income individuals, families with dependent children or adult members, groups and organisations, and those with special needs, such as people with disabilities;

(f) the assumptions made as to consumption and saving patterns and the cost of living for the various 'cameo profiles';

(g) whether the stated objectives of the package can be met by using an alternative and fairer approach; and

(h) such other matters as the committee considers fall within the scope of this inquiry.

(3) That the committee also inquire into and report, on or before 19 April 1999, on the broad economic effects of the Government's taxation reform legislation proposals with regard to the fairness of the tax system, the living standards of Australian households (especially those on low incomes), the efficiency of the economy, and future public revenues, including:

(a) the effects on equity, efficiency and compliance costs of including, or not including, food or other necessities of life in the GST, together with any related adjustments to the package if food or other necessities of life were GST zero-rated;

(b) the effectiveness of the package in easing the poverty traps facing people on low incomes, and reforming and streamlining tax and income support for families with children, taking into account the static and life-cycle impacts on families with children;

(c) options for amending the income tax schedule to make it more equitable;

(d) the findings of the Tax Consultative Committee chaired by David Vos;

(e) options for improving the effectiveness and fairness of the tax system and reducing inequitable or unreasonable tax avoidance and minimisation, including consideration of alternative areas for tax generation, either where there are current tax concessions or where Australia's taxation system does not address major tax potential, and without limiting the foregoing, the consideration of taxation of foreign companies operating in Australia, including the relative merits of resource rent taxes, royalties or land taxes as compared to company tax in securing a fair compensation to Australia for use of its resources, whether the 150% tax concession for research and development should be restored and whether small companies should be allowed to be taxed as partnerships.

(f) the potential for tax avoidance and evasion, including an examination of the effects on the cash economy, and the potential impact of electronic commerce on the future viability of a GST;

(g) the effects on compliance costs;

(h) the potential for reducing payroll tax, including by providing incentives to create long-term employment and by replacing payroll tax with a carbon tax;

(i) whether there are other means available for rebating or reducing the indirect taxes or excessive user charges embedded in exporters costs;

(j) excises, including those on fuel, tobacco and alcohol - identifying the industries which benefit, and to what extent, from the proposed changes to taxes on fuels;

(k) the effects on interest rates;

(l) the effects on investment, in both physical and human capital formation;

(m) the effects on small business;

(n) the effects on the non-profit sector, including the total amounts of money contributed by the sector, administrative costs, impacts on the viability of the organisations, and the consequent effects on the wellbeing of the community;

(o) the effects of the GST on particular industries, including:

- (i) key service industries such as tourism,
- (ii) the Australian automobile and related industries, having particular regard to the effects of changes to fuel excises,
- (iii) other 'invisible' export industries, such as education and financial services, and
- (iv) the international competitiveness generally of Australian industries;

(p) the implications of not requiring that the GST component of goods and services be itemised on receipts;

(q) the effects of the taxation reform legislation proposals on rural and regional stakeholders, including:

- (i) the effects on particular regions,
- (ii) the effects on rural and regional communities of different tax regimes on fuel - especially the cost of transport of goods to rural communities,
- (iii) the effects on primary industry of replacing the current sales tax exemption on agricultural machinery with a GST, and
- (iv) the effects of imposing a GST on food and other necessities of life on remote communities, including Aboriginal and Islander communities;

(r) the effects of the Government's taxation reform legislation proposals on state and local government administration, including:

- (i) the effects of the package on future federal-state financial relations and the capacities of state and local governments to adequately finance their respective responsibilities in both the short-term and the long-term, including the effects of the proposed transfer of responsibility for local government financial assistance to the states, and whether it discriminates between states,

- (ii) the implications for specific purpose programs,
- (iii) mechanisms required to lock in commitments made by federal and state governments with regard to the new arrangements,
- (iv) the implications for future federal-state financial relations of not extending the GST to the necessities of life (such as food, clothing, shelter and essential services) and books, and any adjustments to the proposed arrangements which would be required to federal-state financial relations,

(v) the implications of the package for the quality and affordability of public utility services and for the public utility concessions for social security recipients,
(vi) the effects of application of the GST, and of changes to tax status, on local government and its activities, particularly commercial activities,
(vii) the implications for the delivery of Commonwealth Government services, including employment services, welfare and other social and cultural services, and
(viii) the extent to which the proposed compensation arrangements are secure from change to below adequate levels;

(s) the adequacy of measures to ensure that consumers fully benefit from the abolition of existing taxes;

(t) the effects of the taxation reform legislation proposals on legal and constitutional matters, including:

(i) the constitutionality of the proposed mechanism for future changes to the GST, including whether such changes would present a significant hurdle to future increases, or reductions if deemed necessary to stimulate the economy,
(ii) the constitutionality of the proposed reorganisation of federal-state tax arrangements and whether the powers and functions of states and territories are materially affected by this reorganisation, and
(iii) the effects of the proposals on the cost of access to justice; and

(u) options for amending the proposed legislation to improve its fairness or efficiency.

(4) That, in reporting on the matters referred to in paragraph (3), the committee have regard to the reports of the references committees referred to in paragraph (17) and integrate the findings of those committees into its final report where relevant.

(5) That the committee consist of 7 senators, 3 nominated by the Leader of the Government in the Senate, 3 nominated by the Leader of the Opposition in the Senate, and 1 nominated by the Leader of the Australian Democrats.

(6) That the committee may proceed to the dispatch of business notwithstanding that not all members have been duly nominated and appointed and notwithstanding any vacancy.

(7) That:

(a) senators may be appointed to the committee as substitutes for members of the committee in respect of particular matters before the committee;

(b) on the nominations of the Greens or independent senators, participating members may be appointed to the committee; and

(c) participating members may participate in hearings of evidence and deliberations of the committee, and have all the rights of members of the committee, but may not vote on any questions before the committee.

(8) That the committee shall elect as its chair a member nominated by the Leader of the Opposition in the Senate.

(9) That the committee shall elect as its deputy chair, immediately after the election of the chair, a member nominated by the Leader of the Government in the Senate.

(10) That the deputy chair act as chair when there is no chair or the chair is not present at a meeting.

(11) That the committee have power to send for and examine persons and documents, to move from place to place, to sit in public or in private, notwithstanding any prorogation of the Parliament or dissolution of the House of Representatives, and have leave to report from time to time its proceedings and the evidence taken and such interim recommendations as it may deem fit.

(12) The quorum of the committee shall be a majority of the members of the committee.

(13) The committee set 29 January 1999 as the date for receipt of submissions.

(14) That the committee hold hearings in each state and territory as required.

(15) That the committee be provided with all necessary staff, facilities and resources and be empowered to appoint persons with specialist knowledge for the purposes of the committee with the approval of the President.

(16) That the committee be empowered to print from day to day such documents and evidence as may be ordered by it and a daily Hansard be published of such proceedings as take place in public.

(17) That the following matters be referred to references committees in accordance with the schedule below for inquiry and report by 31 March 1999, and that in undertaking these inquiries the committees have regard to the report of the Select Committee referred to in paragraph (1) and consult widely, holding hearings in each state and territory, as required. Submissions to these inquiries are to be made by 29 January 1999.

Committee	**Matters for Inquiry**
Community Affairs	The impacts of the Government’s taxation reform legislation proposals on the living standards of Australian households (especially those on low incomes), including: (a) the scope and effectiveness of the proposed arrangements on charities, child care services, aged care services, welfare services, local government human services and all not-for-profit organisations in maintaining the quality and affordability of essential community services, including the implications for the public funding of these services and the implications for the commercial activities of these organisations, and whether unconditional GST-free status should apply to *bona fide* charities; (b) a detailed examination of the zero-rating of health services, including an examination of which services should be zero-rated; (c) the effects on community sector organisations of changes to their tax exempt status, and of the compliance costs of the proposed tax arrangements;

	(d) the effects of the proposed private health insurance rebate; (e) the effects on people with disabilities; (f) the effects on public, community and private housing, including the levels of rents; and (g) options for amendments to improve the fairness or efficiency of the proposed legislation.
Employment, Workplace Relations, Small Business and Education	The employment incentive and education impacts of the Government's taxation reform legislation proposals, including: (a) the scope and effectiveness of the proposed zero-rating arrangements for education in maintaining its quality, accessibility and affordability; (b) the effects on employment; (c) the effects of the proposed GST treatment on the quality, accessibility and affordability of employment services; (d) the effects on education of imposing a GST on, or zero-rating or exempting books and associated education resources; (e) the effects on education of imposing a GST on ancillary resources, services and commercial activities, including the effects on overseas students; (f) the effects of the proposed changes to the tax system on employment; (g) the effects on wage costs, particularly if the basic necessities of life are taxed; (h) the scope and effectiveness of changing the unemployment benefits, pensions and Newstart Allowance 'tapers'; (i) the effects of the proposed changes to the tax system on training and adult education; and (j) options for amendments to improve the fairness or efficiency of the proposed legislation.
Environment, Communications, Information Technology and the Arts	The broad effects of the Government's taxation reform legislation proposals on the environment, the arts and information technology, including:

(a) the environmental effects, and likely impacts of changes to fuel excises, particularly but not only diesel, and the replacement of WST with GST on vehicles and other transport services including:

   (i) possible increases in greenhouse gas emissions,
   (ii) increases by amount and type of air pollution,
   (iii) the effects on public and rail transport,
   (iv) the effects on alternative energy use in transport including, but not limited to, compressed natural gas,
   (v) the changed effects on native forests of logging or woodchipping due to the tax package, and
   (vi) the changed effects of mining in environmentally sensitive areas due to the tax package;

(b) the environmental effects of the replacement of Wholesale Sales Tax by the GST and associated changes in fuel excises on electricity and natural gas;
(c) the impacts of the proposed tax changes on the prices and existing and potential use of renewable energy particularly but not only solar energy technology and energy efficiency equipment;
(d) the environmental effects of any changes to taxes on exports;
(e) the consistency or otherwise of the proposed changes in taxation and excise arrangements with Australia’s international treaty obligations, including its obligations under the Framework Convention on Climate Change;
(f) options for a tax system which better achieve environmental objectives,including incentives for fuel efficiency and alternative energy sources, such as measures which promote both environmental protection and employment generation;
(g) the extent to which environmental impacts were considered in the drafting and final copy of the Government’s tax package;
(h) the scope of any consultation on environmental matters with experts in Environment Australia or any other Government departments other than the Treasury and Finance departments;
(i) the impact of a GST on ticket sales for the performing arts;
(j) the effects of a GST on the transfer of grant monies for arts projects;

	(k) the effects of the tax proposals on sponsorship provided by the private sector to individual artists and arts organisations; (l) the extent to which the package will block consideration and introduction of 'ecotaxes'; (m) the effects of a GST on not-for-profit conservation and arts organisations; and (n) options for improving the environmental effects of the package.

(18) That the provisions of the bills implementing the proposed new tax system stand referred to the previously mentioned committees for inquiry and report in conjunction with the terms of reference authorised by this resolution, as soon as the bills have been introduced in the House of Representatives.

(19) That when the bills referred to in paragraph (18) are first introduced in the Senate and a motion is moved for the second reading of the bills, debate on that motion shall be adjourned at the conclusion of the speech of the senator moving the motion and resumption of the debate shall be made an order of the day for 19 April 1999 without any question being put.

WITNESSES

Committee met at 9.10 a.m.

CHAIR—Today the committee continues its inquiry into the first stage of the proposed changes to the Australian taxation system. During the first stage, the committee will focus on the economic theories, assumptions, calculations, projections, estimates and modelling which underpin the government's proposals for taxation reform.

In the second stage of the inquiry, the committee will examine the broad economic effects of the government's taxation reform legislation proposals. It will take regard to the fairness of the tax system, the living standards of Australian households—especially those on low incomes—and the efficiency of the economy in future public revenues.

The Senate referred the inquiry to the committee on 25 November 1998. The committee expects to report on the first stage by 18 February 1999. For three related inquiries by the Senate references committees on Community Affairs; Employment, Workplace Relations, Small Business and Education; and Environment, Communications, Information Technology and the Arts, the scheduled reporting date is 31 March 1999. This committee will then report on the second stage of its inquiry by 19 April 1999, taking into account the findings of the references committees.

This committee called for submissions by 29 January this year and so far has received well over 1,000. This is the first public hearing to be held by the committee in Melbourne in the course of its inquiry. In addition to this hearing, the committee will be conducting other public hearings in capital cities and in some major regional centres.

The committee does not intend to release all submissions as yet, except for the submissions by witnesses who are giving evidence. It is the wish of the committee that submissions 83, 83A, 122, 343, 553, 604 and 605 be made public. I now declare that those submissions to this inquiry, together with their attachments, are to be released.

For the record, this is a public hearing. As such, members of the public are welcome to attend. Before we commence taking evidence, let me place on record that all witnesses are protected by parliamentary privilege with respect to submissions made to the committee and evidence given before it. Parliamentary privilege means special rights and immunities attached to the parliament, or its members and others, necessary for the discharge of the functions of the parliament without obstruction and without fear of prosecution. Any act by any person who operates to the disadvantage of a witness on account of evidence given by him or her before the Senate, or any committee of the Senate, is treated as a breach of privilege.

[9.13 a.m.]

BLANDTHORN, Mr Ian, National Assistant Secretary, Shop Distributive and Allied Employees Association

CHAIR—Welcome. I invite you to make an opening statement if you wish and to be available for questioning from the committee.

Mr Blandthorn—The SDA is Australia's largest single union, as many senators would be aware, with over 230,000 members. Most of those people are low income earners. Most of them live in low income families. Many of them are women; many of them are young people. We have made this submission because we are concerned about the implications of the proposed tax package for those members and their families, and for other people also in similar positions to them.

When we put this submission together, we did so in the belief that major reforms such as this should be governed by certain core principles, that government should take into account certain core principles in the introduction of major change in these areas. Consequently, we have put to the committee that it is imperative that, firstly, the government recognises that the family is the basic social unit of our society and should be supported by governments; secondly, a standard of living which allows people to have a decent living style is a right of all Australians and should be recognised in any reform that is implemented; and, thirdly, any changes should take particular note of the needs of those least well off in our community.

The SDA has been concerned with the proposed introduction of the tax package because, in our view, it is inequitable and also economically inefficient. It is our belief that, if this package were introduced in the form that is currently proposed, it would provide significant disadvantages to low income families and significant advantages to those on higher incomes. Therefore, we regard the package as highly regressive.

The mere introduction of a GST will fuel inflation. It must inevitably increase the cost of living. There may be some debate as to what the cost of living increase will be but, nevertheless, there must be an increase in the cost of living. We would suggest that while the figure of 1.9 per cent has been mentioned in a number of the papers issued by the government, most observers regard that as a gross understatement of the likely CPI impact and expect that the figure will be much higher than that.

Low income families, such as members of the SDA, effectively spend all of their income in order to meet their needs to sustain themselves at a viable living standard. They do not have discretionary income. Those on higher incomes do have discretionary income; they do have the capacity to save if they wish to. In our view, those who have the capacity to save will benefit from this package because they do have the benefit of having income which opens them to choice as to how they may spend it. Low income families do not have that. If there is an increase in the cost of living, given that low income families are already spending all of their income in order to meet their needs, this must have an impact on the standard of living that those low income families experience.

If there is an increase in the cost of living, if members find themselves worse off as a result of this package, if they find that the compensation is not adequate—and we are yet to be convinced that it is adequate—then senators should not be surprised if unions make new and fresh wage claims in the future.

There is no evidence, in our view, that a GST will increase employment. My particular concern is with the retail industry and the people working in the retail industry. I want to look at some of the potential implications for the retail industry and its workers with the introduction of a GST. If prices rise, then it follows that consumers will buy less. Last year, Coopers and Lybrand conducted a survey of retailers on their views in respect of the introduction of a goods and services tax. That survey is mentioned at some length in the submission we put to the senators. In brief, that survey shows that a majority of retail employers have the view that a GST will be bad for their business and that a GST will lead to reduced expenditure.

Some of the features of that survey show that 100 per cent of pharmacy, health and beauty retailers believe that there will be reduced expenditure in their sector if a GST is introduced; 90 per cent of food and liquor retailers have a similar view; 79 per cent of the apparel retailers have a similar view; 75 per cent of category killer retailers have a similar view, and most other retailer areas are of a similar view as well. In our view, that represents an overwhelming vote of no confidence by retail employers of the proposition of a GST.

In August last year the *Retail World* magazine, which is one of the trade magazines for the industry, commissioned the Dairy Marketing Group Pty Ltd to conduct a survey of grocery buyers throughout Australia on their attitudes to a GST and on how they considered it would impact upon their shopping habits.

Over half of those surveyed were opposed to a GST on food. Opposition was from across all the various demographic groups. Opposition was especially strong among low income respondents. Those respondents indicated that a GST would be likely to lead them to change their shopping habits by purchasing less, by cutting out luxuries, or by changing to cheaper brands. Clearly, a GST will have an adverse effect upon the retail industry. Consumers will restructure and reduce their spending.

The retail industry is not noted for having superfluous employees. It is often regarded as and called a lean and mean industry. It employs the number of people that the retailers at any given time think they need, but no more than that. It is our view that if spending patterns are changed, if spending is reduced, that will lead to reduced employment in the industry.

In the first instance it would probably lead to part-time and casual workers having their hours cut. In recent times there has been a huge debate in this country, and it is still going on, about youth employment. In our view a GST will cost young people their jobs. A GST will lead to lower employment levels in the retail industry, and some people will experience reduced hours or no hours as a result.

We simply do not believe that in terms of the retail industry there are any employment benefits, only employment negatives, from the introduction of a GST. I would suggest to the senators that those who argue there are going to be employment benefits from the introduction of a GST have the onus put on them to prove that will be the case because the indicators do not suggest that that is the situation at all.

A GST will adversely affect education, especially vocational education and training. Are trade magazine, trade manuals, tools and uniforms that people are required to purchase to learn their trade, to do their job, covered by a GST? The answer in those cases is yes. Already young people who are trainees or apprentices are on extremely low wages; many are struggling to make ends meet on the wages they are on. Increased costs will mean that some young people simply will not be able to access apprenticeships and traineeships. Increased costs will have the effect of turning people away from trade training. Increased costs will have a serious long-term implication for the skill base of this country.

The GST will impact on various charges relating to health, housing and child care. When you add those increased costs relating to health, housing, education and child care to the increased costs of purchasing the daily necessities, then the introduction of a GST has to be seen as anti-family.

The second issue that I want to mention briefly is the issue of poverty traps. The tax papers make some mention of trying to deal with the effective marginal tax rates. There is now wide recognition in our society that we do have a huge problem with effective marginal tax rates because of the lack of integration between the social security and taxation systems.

The people at NATSEM have done a lot of work on this, and I am aware that they appeared before this committee several days ago. One of the surveys conducted by NATSEM, and issued last year to a conference of economists, showed that for many families the joint impact of tax and overlapping means tests meant that there is little benefit often for the second income earner to be in the paid work force at all. Yet, conversely, most families these days need both spouses in the paid work force in order to meet their needs economically.

So families are caught in a bind. On the one hand they have to have both spouses in the paid work force and, on the other hand, they experience the effective high marginal tax rates, particularly as it applies to any government entitlement such as family payments they might otherwise seek to claim.

The package also refers to trying to provide benefits to families. But we point out to senators that over the last two decades—since the Fraser government first introduced family allowances back in 1975—there has been an erosion, and there continues to be an erosion, of the value of family payments. That, combined with the impact of high effective marginal tax rates, means that many low income families are no longer able to access basic income support payments that once were regarded as their right, and which they often need in order to survive economically.

Certainly, the government does, to some extent, address the issue of high effective marginal tax rates in the tax papers. We acknowledge that there will be a reduction in the effective marginal tax rates if the package is introduced. As was shown in the *Financial Review* by Alan Mitchell, those effective marginal tax rates will be reduced from around

86 per cent back to around 75 per cent. But they will still be there and they will still be extremely high. While we applaud the government for at least recognising that there is a problem with effective marginal tax rates, we say that the package does not go anywhere near far enough in addressing this very serious problem.

The third issue that I wish to mention is the tax cuts themselves. The most generous tax cuts under the new scales apply to those with incomes over $38,000. Lesser cuts go to those under $38,000. I point out to senators that, in many cases, the people most adversely affected here will be young people and women because they constitute a disproportionate share of those earning incomes below $38,000.

If one looks at the impact of the tax cuts, a single person on $75,000 receives a tax cut of about $86 a week whereas somebody on $20,000 receives a tax cut of $10 a week. The net benefit on the $20,000 income is just 1.3 per cent compared to 7.3 per cent for the $75,000 income. We are not saying the dollar figure should be the same but, certainly, there is no equity at all in the way that those tax cuts have been framed.

Fourthly, we are—

CHAIR—Mr Blandthorn, I do not want to interrupt your flow but the committee has a number of questions. How much longer do you think you will need?

Mr Blandthorn—Could I have another two minutes?

CHAIR—Right, please proceed.

Mr Blandthorn—I am almost finished. There is only one issue I still wish to raise. It relates to the social wage implications of the tax package. On one hand the tax papers suggest that there will be benefits to business as a result of the package. The benefits to business will be at least three per cent. On the other hand there are substantial tax cuts. If business has tax cuts and individuals have tax cuts—noting that the highest tax cuts go to those on high incomes—what are the implications for government revenue? What are the implications for social wage expenditure in the future?

It seems to us the only choice available to the government would then be, given that there must inevitably in such a situation be a reduced public revenue, to incur a higher deficit to maintain expenditure on the social wage or, otherwise, reduce social wage expenditure. Again, those most affected would be those on low incomes.

Senator, I will stop there.

CHAIR—Thank you very much. Senator O'Chee.

Senator O'CHEE—Mr Blandthorn, let us start with child care. If what you say is correct it sounds pretty serious. You say on page 21:

> The cost of many items used in child-care centres, from nappies to toys, to milk and bottle formulas, will be subject to GST.

Is that what you say in your submission in the second paragraph, second sentence?

Mr Blandthorn—Yes, Senator.

Senator O'CHEE—I suppose we are talking about things like Lego, playdough and things like that being subject to GST?

Mr Blandthorn—That is my understanding.

Senator O'CHEE—That is your understanding? You put it in your submission, is that correct?

Mr Blandthorn—Yes.

Senator O'CHEE—First of all, are you aware that Lego, playdough, stuffed toys and all children's toys are currently taxed at 22 per cent?

Mr Blandthorn—Yes.

Senator O'CHEE—Why did you say that this would be detrimental to child care when these items are already taxed at 22 per cent?

Mr Blandthorn—Senator, what one has to look at is the global picture, not try and isolate individual items.

Senator O'CHEE—The global picture is that these are becoming cheaper.

Mr Blandthorn—If one looks at the global picture and looks at the impact of a GST across the range of items required in child care—whether it is in a child-care centre or caring for children at home—there will be a significant cost impact.

Senator O'CHEE—Mr Blandthorn, you said:

The cost of many items used in child-care centres, from nappies to toys, to milk and bottle formulas, will be subject to a GST.

Yet you admit you actually knew that those items were already subject to a wholesale sales tax of 22 per cent?

Senator CONROY—Yes, and that price will go up. Haven't you heard of retail mark-up?

CHAIR—Order! One questioner at a time, please.

Senator O'CHEE—Thank you, Mr Chair. Mr Blandthorn, you then responded to my question by saying, 'You've got to look at the global effect.' Do you accept the fact that child care is GST free and is stated to be GST free in the tax package?

Mr Blandthorn—I have seen those words, Senator. I must say to you that I challenge whether in fact that is an accurate statement.

Senator O'CHEE—On what basis do you say that?

Mr Blandthorn—It may well be that child-care fees will be GST free.

Senator O'CHEE—Do you understand what a GST free industry means?

Senator CONROY—Rents weren't meant to go up and they are GST free.

Senator O'CHEE—Listen, Senator Conroy, you are not the witness.

CHAIR—Order! Let's not have any debate between the committee members. This is an opportunity for the witness to put their evidence before the committee. The debate will be later. Please proceed, Senator O'Chee.

Senator O'CHEE—Do you understand what a GST free industry actually is?

Mr Blandthorn—Yes, Senator.

Senator O'CHEE—What do you understand a GST free industry to be?

Mr Blandthorn—I do not believe there will be any GST free industry.

Senator O'CHEE—Mr Blandthorn, clearly the tax package says that an industry which is GST free will have all the GST rebated on its inputs and will not charge GST. Do you accept that will be part of the package?

Mr Blandthorn—I acknowledge that those words are in the tax papers.

Senator O'CHEE—Why do you think it is going to be any different? Do you think that maybe Senator Harradine is going to decide to impose GST on child care?

Mr Blandthorn—I have no idea what the Senator might do.

Senator O'CHEE—You are saying you admit that those things are in the package but you do not believe there is going to be any GST free industry?

Mr Blandthorn—I acknowledge that the government has said that certain areas will be GST free. When one analyses, however, where the GST will apply then one comes to the conclusion that, while certain features may be GST free in relation to an industry, there will be other features of that industry where the GST has an impact.

Senator O'CHEE—Such as?

Mr Blandthorn—I think child care is a classic example.

Senator O'CHEE—Where? I am giving you the opportunity to tell me. Where?

Mr Blandthorn—I think if one looks at the area of child care a lot of the things that people need to care for children will in fact be subject to a GST.

Senator O'CHEE—In referring to child-care centres, you said this is a tax on child care. Where will the tax be imposed on the operating costs of a child-care centre?

Mr Blandthorn—Senator, if we are talking about operating costs as fees, that might be one thing. If we are talking about operating costs as anybody utilising a centre would understand them, which includes all costs—everything which is an input into that centre—then a lot of those things will be subject to a GST.

Senator O'CHEE—And the GST is rebated in full because it is a business input. That is the essence of a GST free industry. Obviously, Mr Blandthorn, you do not understand that.

Mr Blandthorn—Senator, if in fact what you are saying is the case, then my concerns are even greater. What you are suggesting is that if I put my child in a child-care centre and that child-care centre uses nappies on my child, then I will get a rebate for it. But if I care for that child at home and purchase the nappies myself, will I still get a rebate?

Senator O'CHEE—Mr Blandthorn, you now accept, I understand, that every business input in a child-care centre has the GST rebated in full.

Mr Blandthorn—Senator, I hear what you say. I do not accept that that in fact will be the way it works.

Senator O'CHEE—Do you accept that it is in the package? Yes or no?

Mr Blandthorn—I am not sure that it is clear in the package, Senator.

Senator O'CHEE—We will give you the information package after. Let us move on to some of the other things you have said. You said that your union opposes the imposition of any what you call 'regressive' taxes. Is that correct?

Mr Blandthorn—Yes, Senator.

Senator O'CHEE—That is the policy of your union?

Mr Blandthorn—Yes, Senator.

Senator O'CHEE—When wholesale sales tax was increased across the board by two per cent by the previous government, what complaint did you make?

Mr Blandthorn—Senator, we have not said in our submission that the current system is perfect. We acknowledge that there is a case for reforming the system. We acknowledge that there are problems with the sales tax system. What we are questioning is whether in fact the introduction of a GST will address the problems that currently exist.

Senator O'CHEE—I am just asking you—you said it was the policy of your union to oppose the imposition of any regressive taxes. I am just wondering what the consistency of your position is. What complaint did you make to the previous government?

Mr Blandthorn—Senator, our concern with the introduction of a GST is that it will impact by increasing costs in a range of areas that will most adversely affect our members in a way that they have never affected before because it will impact on the necessities of life.

Senator O'CHEE—Mr Blandthorn, I will ask you the question again. I am trying to be as reasonable about it as I possibly can be. What protest, if any, did you make to the previous government when they imposed a raft of regressive tax increases on wholesale sales tax?

Mr Blandthorn—Senator, in respect of the last increases in sales tax, we probably did not make a submission of the nature that we are making here today. I acknowledge that.

Senator O'CHEE—Thank you.

Mr Blandthorn—Again, Senator, let me say that what is being proposed here is in magnitude so vastly different to what occurred when the wholesale sales taxes were last increased that there can be no comparison between the two because the impact here will be so much greater.

Senator O'CHEE—Mr Blandthorn, you said just a moment ago that you do not believe the existing indirect tax system is fair. You just said—

Senator CONROY—He has never said that.

Senator O'CHEE—Mr Chairman, can I please just ask questions of the witness without interruptions?

CHAIR—Order. Proceed, Senator O'Chee.

Senator O'CHEE—You have just said that you do not accept that the existing sales tax system is fair. How would you change the existing sales tax system to make it fair?

Mr Blandthorn—Senator, what I said was that we acknowledge that there are problems with the current system.

Senator O'CHEE—So what are those problems?

Mr Blandthorn—And what we have said in our submission is that there are a range of initiatives that need to be introduced to bring about a fair taxation system. You cannot—

Senator O'CHEE—How would you fix the sales tax system?

Mr Blandthorn—Senator, if you will allow me to answer the question.

Senator O'CHEE—Please.

Mr Blandthorn—What we are saying is that, if you are going to address the issue of taxation, you need to address it as a big picture item. You will need to address the whole system. That is why we have concentrated in our submission on dealing firstly with core principles, dealing with what ought to be the features of a tax system, and then about some of the changes that need to be introduced.

There may well need to be changes to the sales tax system. I do not move away from that. I am not saying the current sales tax system is perfect, nor do I claim to sit here and have all the answers. What I do sit here and say is that the introduction of a GST is going to severely impact upon low income families.

Senator O'CHEE—You also say that vocational education will be taxed under GST.

Mr Blandthorn—Yes.

Senator O'CHEE—But you are aware that vocational education is GST free, just like child-care centres.

Mr Blandthorn—Again, it is the same issue that you raised with child care. Fees may be GST free, but what I have questioned is whether a number of the inputs critical to vocational education and training will be GST free. I ask: will trade manuals be free? Will the tools people are required to purchase to learn a trade be free of GST?

Senator O'CHEE—If you read the tax package, you will know that all the inputs to vocational training, including the tools people will be using and the books used by the colleges, are all GST free.

Mr Blandthorn—I do not think that is at all clear from the package, Senator.

Senator O'CHEE—Mr Blandthorn, what we will do is send you the package again and highlight the relevant bits.

Mr Blandthorn—Thank you, Mr Chairman.

Senator MURRAY—You have stated, if I can summarise it, that the imposition of the GST will increase inflation, decrease jobs and affect growth detrimentally. The Treasury last week released figures which showed that, if food was taken out of the GST, inflation rates would drop from 1.9 per cent to half of one per cent. I think it was Murphy the modeller's last phrase. Murphy the modeller said that, if food is taken out of the GST, it will not affect growth rates detrimentally—in other words, the same GDP effects will occur. What is your view of the GST if food were to be taken out?

Mr Blandthorn—I think either you have a GST or you do not. The problem I have with isolating food is that it is simply one component of a number of things that families need in order to survive. People also need housing and clothing. If a GST remains on those things, even if you isolate food, the impact is still substantial, particularly on those with little or no discretionary income.

I really take the view that it is a broader issue than just trying to isolate food. If the GST is not going to be across-the-board, then it really should not apply to anything that ought to be regarded as a necessity of life, so it should not apply to housing and clothing and so forth. I do not take the view that food can be isolated from the other necessities.

Senator MURRAY—So you take the pure view of GST policy that it should be across-the-board and not have isolated exemptions?

Mr Blandthorn—I could support exemptions if they were exemptions for all the areas that people needed in order to lead a decent standard of living. The problem I have is in simply isolating food.

Senator MURRAY—But the government has already isolated education, health and financial services. Out of 18 OECD countries that put a GST on, 14 do isolate food. They either zero rate or low rate it. Why do you take a view, therefore, that food does not matter when it is such an important component in the lives of families and low income persons?

Mr Blandthorn—I am not saying food does not matter, Senator. I think it matters a lot. Those people who argue that food ought to be isolated from a GST are coming at it from basically the right perspective. The view I have, however, is that there are other necessities of life that people need. I have a problem with isolating food while the GST remains on those other key areas.

Senator MURRAY—I think your submission says you have 230,000 members. Have you surveyed them to establish, firstly, whether they will oppose the GST or believe you should oppose the GST; and, secondly, if the GST were to pass, whether they would want it modified in any particular way?

Mr Blandthorn—We have certainly spoken to our members at great length on the first issue about whether they would support or not support a GST. I certainly come here today with strong resolutions and my organisation behind me, having no doubt that our members support us in the submission we are putting here to effectively say to the senators that people need certain things in order to live a decent standard of life and those things should not be subject to a GST.

Senator MURRAY—The polls and surveys done on the food issue indicate that between 60 and 70 per cent of all Australians oppose a GST on food. Do you think that would be reflective of your members as well or have you any way of knowing whether that is reflective of your members?

Mr Blandthorn—The survey that we included in our submission supports what you have just said that the majority of consumers are certainly opposed to a GST on food. I have spoken at length—and other union officials have spoken at length—to our members on this issue and I have no doubt that they are strongly opposed to a GST on food. But they would also be opposed to a GST impacting upon their purchasing of clothes or their rents or their purchasing of homes as well.

The other survey of retailers that we included in this document that we have put to you shows that right across the board retailers expect that there would be a reduction in expenditure by consumers if a GST were imposed. That has very substantial implications for employment in the industry and it is one of the reasons why our members are so strongly opposed to a GST.

Senator MURRAY—Is that view short term, medium term or long term? You know the whole business about the pass through effects and when the price impacts occur. Is the survey response that the reduction in consumer expenditure will be principally short term or over a longer period?

Mr Blandthorn—I think the way the survey was framed, it asked what people would do, not what people would do in the short and long term.

Senator MURRAY—In section 7: you have itemised some desirable reforms. I think the purpose of this committee is three-fold: primarily to examine the government's package; secondly, to see if any modification or improvements should be made to it; and, thirdly, to suggest alternative remedies for the Australian tax system.

You proposed two areas in particular which are noteworthy. One is a wealth tax and the other is a minimum corporate tax rate. Dealing with the minimum corporate tax rate, what is the minimum you think all corporations should pay or have you done any modelling on it?

Mr Blandthorn—No, we have not done any modelling, and we do not have a firm view about what the minimum ought to be, except to say that there should be one.

Senator MURRAY—Do you think that a gigantic multinational corporation—who, for instance, the Taxation Office were very proud to have lifted from an effective tax rate of nine per cent to 11 per cent—would be paying too little?

Mr Blandthorn—One of the things that concerns us is that a whole range of major corporations in this country is able to pay far less than what we would regard as a fair share.

Senator MURRAY—And the burden falls too much on the PAYE earners?

Mr Blandthorn—Absolutely.

Senator CONROY—Is it the case that your organisation represents hundreds of thousands of low income workers, Mr Blandthorn?

Mr Blandthorn—Yes.

Senator CONROY—Would you give us a bit of a profile of your membership and their circumstances?

Mr Blandthorn—We have got over 230,000 members. About two-thirds of those would be women. Many of them would be young people under the age of 21. In 1996 we had independent consultants do an extensive survey of our members for us. That survey indicated that the vast majority of our members are not only low income earners—which we know because wage rates in the retail industry are not high by any comparison, and I am not aware of anyone who argues that they are—but also they live in low income households.

Senator CONROY—What is the average income we are talking about?

Mr Blandthorn—The retail industry is characterised by part-time and casual work. A lot of the income earners in our membership profile are in fact second income earners. You cannot sustain a family on a part-time or casual income. Many of those incomes are therefore in the $100 to $200 range. The normal wage rate for a shop assistant who is working full-time is somewhere between $430 and $500, depending on whether it is an award rate or whether it is an enterprise agreement rate. The survey showed that the families of the vast majority of our members have disposable incomes of less than $700 a week.

Senator CONROY—With your enormous experience and involvement in the sale and distribution of goods and services, do you consider it credible that all businesses in Australia will pass on all the cost reductions that they are going to receive to their consumers?

Mr Blandthorn—I would suggest, anecdotally, that if one looks at what has happened in this country in the past, one would see that that has never been the case. Why would it be different next time around?

Senator CONROY—Treasury are assuming 100 per cent pass through.

Mr Blandthorn—It is very easy to set up a model and make those sorts of assumptions. Whether the reality will be the same as the model is questionable. I do not know whether it will or will not be. I have my own views that I have just expressed. I think it is incumbent upon those who would propose change to demonstrate that there is validity in their assumptions, and I am not sure that that in fact has been done.

Senator CONROY—Your submission assumes that the real first-year impact on most workers will be much higher than the inflation figure the government uses. Could you elaborate on that?

Mr Blandthorn—The government has indicated that in some areas it will use the four per cent figure as the compensation base. It has also indicated in other areas that it will use the figure of 2½ per cent as the compensation base. Whether the government uses one or the other, I think when one looks at the models the Treasury has put up in recent times one will see that there appears to be an underestimation of what the real effect will be. Therefore, we are concerned that the models are based on an underestimation of what the real cost of living increase will be.

Senator CONROY—If the inflation rate is higher, as you suspect, than the figure the government told the people before the last election, that is, higher than the 1.9 per cent that they are assuming, do you expect there will be pressure for wage increases to offset this new burden?

Mr Blandthorn—There are two issues there. Firstly, you are asking whether if in the short term the compensation rate fully addresses the CPI increase, will the compensation rate maintain its real value over time? There are no indications that it will. That is one point.

Secondly, as I said before, we are not convinced that the compensation rate proposed by the government will fully meet the CPI increase. If there is a problem, short-term or long-term, with the compensation rate, then inevitably workers are going to conclude that they are worse off. It will be low income families that will be affected first because of their lack of discretionary income. Therefore, as we have indicated in our submission, people should not be surprised if at some stage in the future, if the compensation rates are inadequate, workers do put demands on employers for increased wages. It is, certainly, a serious option that must be considered by the Senate, that the introduction of the GST will lead to new wage demands in the future.

Senator CONROY—Your submission states on pages 14 and 15 the results of a survey of retailers—I think conducted by Coopers and Lybrand—about the effects of a GST. Could you just expand on what you have already said on that issue, in terms of what the survey says?

Mr Blandthorn—I am not quite—

Senator CONROY—It is on pages 14 and 15.

Mr Blandthorn—That was a survey conducted by Coopers and Lybrand last year. It was a survey of retailers representing more than 50 per cent of retail sales nationwide. It was clearly a very comprehensive survey. It showed that 51 per cent overall believed that a GST would reduce spending. But when you look at the number of retailers in particular categories who believe that there would be a reduction in spending, then that is where the real concern is because 90 per cent of food and liquor retailers and 83 per cent of supermarket retailers believe there would be a reduction in expenditure. In other words, people will have to cut back on the necessities of life because of increased costs.

Senator CONROY—What has been your organisation's experience in the retail sector when retail spending has fallen? Would this mean jobs?

Mr Blandthorn—Only last week I had one retail company come to me and indicate that it had suffered a substantial decrease in sales and was going to therefore make a 10 per cent across-the-board reduction in working hours for its staff nationwide. That is what happens when there is a reduction in spending—working hours are cut and people lose jobs.

Senator CONROY—The GST will inevitably rise, as we know from international experience. This is another reason why Labor has always opposed the GST, that and its impact on low income families. Does your association agree? Have you got any international experience about the GST and equivalents rising?

Mr Blandthorn—One of the points we make in our submission is that there is no guarantee in the tax papers that once a GST is introduced it will not increase. If one looks internationally, GSTs, and propositions similar to GSTs, have often been introduced at one rate and then increased. We have grave concerns as to where a GST, once it is introduced, may finish.

Senator CONROY—We have heard a lot from the Treasurer and the government about how a GST will be a transparent tax. It is one of the arguments that they have championed. However, he has falsely claimed that consumers would know how much GST they would be paying. We now know that the government is intending to hide the GST as they voted against an amendment of ours in the parliament recently that would have seen it listed on retail dockets. It seems to me that hiding the amount of a GST will mean that retail employees will often be held to blame by consumers for the increase in prices. Does that concern you?

Mr Blandthorn—We make the point in our submission that the introduction of a new tax which leads to increased costs of goods and services will hit consumers. In many cases, the first time consumers are hit with those costs they are going to be surprised. The people at the front, that is, the shop assistant serving the customer, is the person we are concerned for. We believe that once a GST is introduced, people will take out their anger on the people serving them. That is why we ask in our submission whether anyone has considered the impact of the GST on those people at the front line, those people actually serving the consumers, when they are suddenly open to abuse and criticism because of something that is beyond their control. They are the only people that consumers can take out their ire on.

I must point out to senators that already our members suffer a great deal of criticism and scolding from customers in shops now when things do not go right. We are concerned that this will exacerbate that situation substantially.

Senator CONROY—Thank you.

Senator FERGUSON—If I could just take up your last point, Mr Blandthorn, I presume you have connections with other unions of a similar kind around the world. Can you tell me whether you base your statement that shop assistants will have to deal with angry customers because of increased prices stemming from the introduction of a GST on international experience where other GSTs have been introduced?

Mr Blandthorn—I base it on my experience of what has been the situation in the retail industry for many years, that when consumers are unhappy, the people they take their anger out on are the people at the checkouts. Again, in the future, if people are unhappy with something, we are concerned that the people they will take out their anger on are the people at the front line.

Senator FERGUSON—How many of your 230,000 members would actually be working on checkouts? I would have thought they worked in all sorts of areas throughout shops and allied industries.

Mr Blandthorn—Absolutely, but you have only got to go into a shop, and whether it is a supermarket with a checkout at the front end or a department store with cash registers dotted around the various floors of that department store, our members are still serving customers. It is at that point, where they interface with a customer, that we have concerns if a system is introduced that consumers are not going to be overwhelmingly happy with.

Senator FERGUSON—From my experience, I have been in butcher shops where the price of meat has sometimes gone up by $1 a kilogram, which is in the order of a 12 or 15 per cent increase, and people accept it. Prices in shops are going to go up nothing like that amount. You have already heard what the anticipated CPI effect is, even if you think it is going to be a bit higher. So what are these terrific price rises that you are talking about that people are going to be angry about?

Mr Blandthorn—Senator, any increase leads some people to be upset; other people take it in their stride. I think the people who are going to be the most upset are those with the least amount of discretionary income where every dollar counts.

Senator FERGUSON—But you have no evidence to prove it; it is just an anecdotal statement.

Mr Blandthorn—Absolutely, but I do point out that, while it is anecdotal, it is based on experience of what has been going on in the retail industry for many years, where members already are subject to constant criticism from many consumers for a range of things that consumers are not happy with.

Senator FERGUSON—Lots of the way through your submission you have used the word ‘anecdotal’ or ‘anecdotally’ quite a bit. Do you think governments should make their decisions on anecdotal evidence?

Mr Blandthorn—No, I do not. In fact I think the exact opposite. I think governments should make their decisions based on facts and that is why I have tried to stress that I think that it is incumbent upon the government, if it wants to introduce a new tax system, to answer conclusively all the questions that are being raised.

Senator FERGUSON—The government has to use facts, but when you are giving evidence, we have to take notice of your anecdotal evidence?

Mr Blandthorn—No, what I am saying is that I think that, if somebody wishes to introduce a change of the magnitude of a GST, it is incumbent upon them to demonstrate at the end of the day that people will be better off and better off in an equitable way than they are with the current system. I am not convinced that the government has done that in respect of this proposed tax package.

Senator FERGUSON—You said the CPI effect would be much higher. How much higher? You must have some evidence as to what you think it will be.

Mr Blandthorn—I am not an economic modeller. I do not pretend to be. I do note that commentators consistently have pointed out that they expect the impact of the CPI to be greater than what the Treasury has estimated it to be. I think that raises a serious question if there is doubt as to what the final impact will be. I think it is incumbent upon the government to remove those doubts as to what the impact will be before a new system is introduced.

Senator FERGUSON—Would you not say the government has gone a long way to removing that doubt when it has guaranteed that the compensation will be 1.5 per cent above whatever the eventual CPI impact is? It is part of the package.

Mr Blandthorn—The tax papers also point out what levels of compensation there will be. If the modelling is wrong, then that compensation may not be adequate. Even if the compensation is adequate today, will it be adequate next year and the year after?

Senator FERGUSON—You have missed my point. It has said that currently the package compensates at four per cent. If the actual CPI is higher than the 1.9 that is quoted by the government, then the government has said in its package that, whatever the actual CPI is, the compensation factor will be 1.5 per cent above the actual CPI impact. What better guarantee can you have than that?

Mr Blandthorn—If the compensation package is introduced at a particular figure the day the GST is introduced and the actual impact is greater, what happens then?

Senator FERGUSON—They will be compensated at 1.5 per cent above the actual rate of CPI.

Mr Blandthorn—When?

Senator FERGUSON—Once the package is introduced. I move to another point that you have made when you have talked about surveys because you have 230,000 people. We asked you whether you had done a survey and you said you had spoken to your members. I presume you have not spoken to all 230,000. What sorts of surveys do you do of your members to find out how they actually feel? You say that in surveys that have been done a majority of people are opposed to the introduction of a GST. Can I suggest to you that if you had done a survey in 1993 of all of your members and asked them if they were in favour of the then government adding two per cent to the wholesale sales tax system, they would all have said, ‘No, we don’t want them to add two per cent to the wholesale sales tax system.’ Have you ever known a survey to come out in favour of any changes to the taxation system?

Mr Blandthorn—I do not think any survey—again this is anecdotal and I am remembering your point of a minute ago—would come out and suggest that people would like increases in taxation.

Coming back to your original point, Senator, we did a major survey of our members in 1996, for example, where we employed an outside consultant. That was a properly conducted, statistically valid survey. So, not only do we do it internally, we also employ outside consultants to assess our members’ views on a range of issues. We believe that we consult very extensively and, as I said, we have no doubt that what we have put here represents the views of our members.

Senator FERGUSON—You make a great play about the fact that a GST will make every shop assistant a tax collector. As I understand it, under the present system, the small business owner has to remit wholesale sales tax. Under the new system, they will have to remit goods and services tax. What is different about the shop assistant under a wholesale sales system as opposed to a GST system? They are still tax collectors now, aren't they?

Mr Blandthorn—Except in the future with a GST, if it is introduced, these people will have to bear the brunt of the consumers' ire at a GST imposed on what often will be the necessities of life.

Senator FERGUSON—Did they bear the brunt of the wholesale sales tax collection when it went up by two per cent?

Mr Blandthorn—Our members bear the brunt of consumers' anger at everything that people are unhappy about in the stores.

Senator FERGUSON—Somewhere here—I cannot find the exact place—you talk about the price of everything going up. That is the term you use but I have not got the exact page. You do not really believe that everything is going to go up, do you?

Mr Blandthorn—I acknowledge that the government has exempted, or indicated there will be exemptions for, certain areas.

Senator FERGUSON—Not even exemptions; even goods that are taxed currently will not all go up. Some will come down.

Mr Blandthorn—That is right, Senator, but a lot will go up.

Senator FERGUSON—You did not say a lot would go up. I will find it directly but in here you say, 'The price of all goods will rise.' It is simply not a fact, is it?

Mr Blandthorn—Overall, the cost of the basket of goods that people need to survive will increase.

Senator FERGUSON—That is not what you say. All you do is talk about the GST; you do not say anything about the compensatory factors of income tax cuts or compensation to allow for any increases that might occur, which the government, as you know, has calculated at 1.9 per cent. You do not make any allowance for other factors. You talk about a GST but never talk about a package.

Mr Blandthorn—Senator, with respect, that is not true. We do refer to the compensation issue. We do express concerns as to whether compensation will be significant. We do indicate that in fact that could lead to new wage demands if the compensation is not adequate. We do address the issue of the tax cuts. We do point out that the tax cuts are highly inequitable because they provide the greatest benefits to those on high incomes. We do address those issues and we also, in our submission, put proposals for a much more equitable way of dealing with issues such as tax cuts.

Senator FERGUSON—You also, it seems, oppose the abolition of provisional tax?

Mr Blandthorn—That is what we have said, Senator.

Senator SHERRY—Two points: firstly, my colleague Senator Conroy referred to the issue of the government not ensuring in its package of legislation that the GST, where it applies, will be marked separately with the final retail price. Do you believe the legislation that we are dealing with should ensure that the tax is clearly marked on the retail price?

Mr Blandthorn—You would be aware that, in a number of overseas countries, that is the way it is done. It is one of the reasons we are concerned about the impact on our members, because there will be increases; the increases will not be transparent and consumers will not be happy.

Senator SHERRY—Does your organisation believe that, in law, there should be a requirement to ensure that a GST is clearly indicated on the—

Mr Blandthorn—Absolutely.

Senator SHERRY—Secondly, my attention has been drawn to a recent *Choice* magazine article, which was a survey of weekly food baskets in major centres around Australia, including major regional centres. The survey showed, for example, that the weekly food basket figure was $74.94 for Sydney and $75.96 for Melbourne.

With respect to Launceston and Hobart—I come from Tasmania—the average food basket price was 14 per cent higher in Tasmania and certainly higher in the other regional centres of Perth, Darwin and Rockingham than in Melbourne and Sydney. Given the impact of a GST on food, do you believe that the differential in prices of food in the regional centres that I have outlined will go higher, or will it come down or stay the same as a result of a GST?

Mr Blandthorn—We have indicated in our submission that we are concerned for those living in rural areas because that would seem to follow. Already costs are higher. If you add a GST, costs must continue to go up. People living in outlying areas will be further disadvantaged with a GST.

Senator SHERRY—Thank you.

CHAIR—Thank you, Mr Blandthorn, for your evidence this morning. The hearing will now adjourn for a short break.

Proceedings suspended from 10.16 a.m. to 10.31 a.m.

DRENTH, Mr Frank, Executive Director, Corporate Tax Association of Australia Inc.

NENNA, Mr Romano George, President, Corporate Tax Association of Australia Inc.

CHAIR—The committee will now resume its hearing on an inquiry into a new tax system. I welcome to the witness table Mr Nenna and Mr Drenth. Gentlemen, I will ask you, if you wish, to address us briefly on your submission and to make yourself available for questions from the committee.

Mr Nenna—Thank you very much, Mr Chairman. By way of brief opening remarks, the CTA wishes to make known that it is pleased to have been asked to assist this Senate select committee inquiry into the GST and a proposed new tax system. We do recognise the value and importance of the Senate's legislative review role generally, but all the more so when the legislation, as is the case with the currently proposed taxation reforms, has the potential to so profoundly impact on the wellbeing of Australian society.

I have a few comments regarding the Corporate Tax Association itself which will help you to understand its perspective and its part in the overall tax reform debate. Firstly, the CTA is comprised of 107 corporate members predominantly from what has come to be disparagingly referred to these days—to my regret—as 'the big end of town'. But those same members, as the record shows, are also very substantial and increasing contributors to the aggregate taxation revenues of this country as well as to its overall economic prosperity. Our members have invested billions of dollars in the capital of this country and they employ millions of Australians.

Secondly, the CTA is also represented by over 400 individual members who have been invested by their companies with the onerous responsibility of ensuring compliance with the ever-increasingly complex Australian corporate taxation laws. In other words, the CTA members work at a practical level and on a day-to-day basis with Australia's taxation laws that we are debating today.

With this in mind, there are only a few remarks we wish to make by way of opening statement. First, our association wishes to register its strong support for the current review of business taxation, the so-called Ralph committee review. From its exposure at the coalface, our members have for some considerable time been pleading the case for a comprehensive, objective and, to the extent that it is possible, independent review of Australia's business tax system. The reality, which at last seems to be receiving more widespread understanding and acceptance, is that Australia's income tax laws are becoming so voluminous and so complex that, if the trend continues unabated, the system really does face the risk of imploding upon itself.

The repercussions from this current situation are manifested, firstly, in inordinately high compliance costs and, secondly, in contributing to an increasingly uncertain commercial environment which is always a serious inhibitor to business investment and employment.

Our association particularly applauds key aspects of the Ralph committee's initial 'Strong Foundations' paper, but first of all recommends that any review of business taxation must, of necessity, be considered in the broader context of agreed national objectives. Tax is not an end in itself. It impacts on investment, growth, employment and prosperity.

Secondly, any enduring improvement in the system must address the processes of policy development, legislative enactment and tax administration which to date have contributed to the current totally unacceptable situation. Having said all that, the CTA has some reservations about the government's proposals on entity taxation, particularly the proposed deferred company tax system.

My final brief comment at this stage before I invite questions is in relation to the proposed GST. The CTA is a supporter in principle of the introduction of a broadly based single rate goods and service tax to replace the current complex and flawed wholesale sales tax and a plethora of other inefficient and costly state based indirect taxes.

The CTA, however, wants to register that it recognises the legitimacy of concerns by those who seek to exempt food from the GST base. But, essentially, our position at the moment is that we believe that there must be better, more efficient ways of properly dealing with those concerns. Essentially, we suggest that exemptions from the broad based single rate will add exponentially to compliance costs. To us it would appear to be an unnecessarily wasteful and costly option to the extent that benefits would flow indiscriminately to those not sought to be advantaged by the measures.

A more targeted direct and comprehensive compensation package of measures would seem to us to be by far the most efficient and economic way to go. With those brief introductory remarks, both Frank Drenth and I invite comments or questions from senators.

CHAIR—Do you have any comments, Mr Drenth?

Mr Drenth—I have nothing further to add to the statement.

CHAIR—You attached to your submission to this inquiry a copy of a submission from the Business Coalition for Tax Reform. How are you associated, if you are, with that group?

Mr Drenth—The Corporate Tax Association is a member of the Business Coalition for Tax Reform. I have to say we joined rather late in the piece. We decided after the federal election held in October that the Business Coalition for Tax Reform would be a useful forum for advancing the business tax reform that was going to be put in place by the government.

CHAIR—You say that you are unfairly characterised colloquially as 'the big end of town'. The Business Coalition for Tax Reform, as I recall, spent $4½ million advertising before the last election about what it regarded as the need for tax reform. As a member of that organisation, were you associated with those advertisements?

Mr Drenth—No, we were not, Mr Chairman. I should point out that I understand that that advertising campaign was run by a body called Australians for a Fairer Tax. But, as I said earlier, the Corporate Tax Association did not join the BCTR until October of last year.

CHAIR—After the event.

Mr Drenth—That is correct.

Mr Nenna—Without speaking for that group at that time, as an observer of the laboured process of tax reform over many years in this country by successive governments and various bodies, it seemed to me that those failed attempts previously were to some extent attributed to the lack of appreciation and understanding by the community generally of the need for reform, the lack of integrity in the current tax system and the direction that it was going and the severe consequences that would flow. From their perspective it was an essential investment. They wanted to put tax reform on the agenda and get some sort of community understanding because tax reform cannot go ahead without community support. It seemed logical to me that there is a clear understanding of why they committed those resources.

CHAIR—Do I understand that your organisation, in fact, has as its members many of the companies who would be members of the Business Council of Australia and that, in a way, you are another face of the same group?

Mr Drenth—That is a reasonable approximation of it. There is a significant overlap. I would say that more than half of the members of the Corporate Tax Association are also members of the BCA. There are a number of members of other organisations that are not in both.

Mr Nenna—I sought to address that in my opening remarks regarding the CTA. Our corporate members are also members of the BCA to some extent; our individual members really bring a different perspective on tax reform from a practical compliance based perspective. There is that to bear in mind.

CHAIR—Am I right—correct me if I am not—in saying that in fact your organisation represents essentially the treasurers of these major corporations whereas the BCA represents the chief executives of those organisations?

Mr Nenna—Not quite so, Senator. Rather than treasurers, it is taxation managers or taxation executives, if you like.

CHAIR—Is your organisation or any of your member companies involved in making representations to the government on its now publicly released package of amendments to the tax act that you are aware of?

Mr Drenth—The CTA is in the process of canvassing its members about concerns they have on the GST legislation that was released recently. That is proving to be quite an exercise. We are at the stage where we have developed a draft paper which has been circulated to members for their comment. Once that has been done, we intend to approach the government to talk to them about some of the issues.

CHAIR—Last Wednesday, on the front page of the *Australian Financial Review*, a reputable newspaper, there was a report that, essentially, to paraphrase it, the big end of town was putting in private submissions to the government to amend its tax package which it was not prepared to put before this committee. You have to rely on me for the accuracy of that. I think it is an accurate representation of what the *Australian Financial Review* report was saying. Are you aware of any private matters that are being canvassed with the government by your organisation or any members of your organisation that they are not prepared to tell the rest of us?

Mr Drenth—I am not quite sure what you mean by private matters.

CHAIR—Matters that companies might wish the government to move on in amending their package that has been presented to the parliament but which they are not seeking any publicity for?

Mr Drenth—We would say—I have to be careful here—I should not presume to speak for each and every one of my members, but certainly the CTA will be saying nothing to the government in broad terms that it is not prepared to say to this committee. As I said, in relation to the GST legislation, there are numerous detailed issues that people have raised that we will be talking to the government about but I am not sure whether those are issues that this committee wants to look at in detail. Indeed we have not yet finalised our list. It is a work in progress.

Mr Nenna—I read the same report. It was news to me. I did understand that there were many individual direct representations to government in relation to the tax package but the second aspect of that report—that individual companies or the BCA generally were not prepared to speak frankly to this inquiry—was not part of what I understood to be the case.

CHAIR—Would you agree that it would be hypocritical if companies that advertised to all Australia that they should reform the taxation system privately lobbied the government without revealing to the rest of the country that what they were lobbying about were changes to suit their own private needs in tax reform?

Mr Drenth—I would have to say I would be surprised if there were publicly listed companies advocating positions in relation to tax reform which they were not also stating publicly. The issues are reasonably well known. There is a concern about the proposed new entity taxation system and aspects of the deferred company tax proposals. They are probably the two major issues. I would be surprised if a number of individual companies have not approached the government directly.

Mr Nenna—My opening remarks were carefully chosen and I hope that they will be taken at face value. What I said is that we, the Corporate Tax Association, recognise the value and importance of the Senate's legislative review role. Generally, but also in this very important matter of tax reform, that will impact on society in general. We have no problems with that. If we had a problem at all when we confronted the terms of reference it was with their breadth and we were not quite sure of the extent to which to make submissions. Some of the matters that the terms of reference deal with are really matters that we are currently seeking to properly address as part of the review of business taxation, the Ralph review inquiry. We are not through our thinking processes; we are not through fully canvassing all our membership. It was difficult for us at this stage to comprehensively state our case on all aspects that are part of the terms of reference of this inquiry. That was the only hesitation that we had when confronted by the terms of reference and the invitation to appear.

CHAIR—Let me conclude with these couple of last questions before I pass to Senator Gibson. A business organisation was before us last Thursday that said—and, again, this is my representation of what they said—that they had some views that they wished to put to the government that they were not at that stage asking us as a committee to include in our recommendations. They took the question on notice as to whether they would ask us to include in our recommendations as a committee the issues that they were privately taking up with the government. I must say they made it clear what those issues were. They did not hide them but they did not ask us to recommend them either. Are there any issues, as far as your organisation is concerned, that you are putting to the government that, at this stage, you do not wish us to recommend in our report?

Mr Drenth—No, Mr Chairman. In relation to the business tax reform proposals, we need to be mindful of the fact that the Ralph review which has been put in place is expected to release a discussion paper later this month. The discussion paper is expected to canvass a number of the issues that were raised in ANTS, back in August. However, it seems likely that the discussion paper will canvass various different ways of approaching particular problems. The Ralph committee is due to report to the government by 30 June. This discussion paper that is expected to be released later this month is not likely to present strongly concluded views on particular issues. It will be there to generate further discussion. I have got to say that the cement is a long way from being dry.

CHAIR—Sure. This inquiry continues through until it reports towards the end of April. If the cement dries appreciably between now and then, will you be prepared to make your views known to us?

Mr Nenna—I cannot see any reason why we would not. We have made this point in relation to another matter which I could come to perhaps later on. We see that the process of tax reform is fundamentally important. It cannot happen in our view without both Houses being committed to it. To the extent that we are able to persuade senators and government members to our views as to the prescriptions for reform, we will use any forum to put our views and try to convert the unconverted.

CHAIR—Good luck to your efforts, Mr Nenna. I am not sure how well you will succeed but full marks for trying.

Senator FERGUSON—I want to follow up on the issue that you have raised. I am somewhat puzzled by the line of questioning—Mr Nenna might be able to shed some light on it—as to why it should be wrong for any private company or individual to make private representations to the government.

CHAIR—I do not think it is wrong. But, if those private individuals are telling the rest of Australia what is good for them but they are not prepared to tell the rest of Australia what they want, I think there is a degree of dishonesty in their public presentation. That is all.

Senator FERGUSON—I do not want to debate it with the chairman, but can I suggest that during 13 years of a Labor government I would be amazed if the union movement did not make private representations to the government of the day without wishing to make those matters public. I think it is only normal that there are a number of organisations that wish to talk privately with the government without making those discussions public. Would you have considered it something unusual if in fact the union movement, just to name somebody, spoke with the previous government over a period of 13 years in private about matters that they did not wish to make public?

Mr Nenna—It would not surprise me. In my experience, it has gone on ever since I have been involved in this area. All we say is that, in relation to the current debate, the position of the CTA is that it will cooperate with any Senate inquiry on all of its matters. It is not concerned to keep private any of its views on tax reform.

Senator GIBSON—Mr Nenna, to re-emphasise, I understand your organisation is basically comprised of taxation experts from the larger companies and other professionals. Therefore, you are the tax experts from a fairly large slice of the commercial world of Australia.

Mr Nenna—That is correct, Senator.

Senator GIBSON—Secondly, you have emphasised in your submission to us and in your statement this morning the importance of the recognition of the need for overall tax reform in Australia. In other words, the tax legislation is too complicated and getting more and more complicated. Looking back over the last 20 years, it is getting much more complicated and cannot go on.

Mr Nenna—Absolutely.

Senator GIBSON—The government has proposed a reform of that. Can I get to, if you like, the nitty-gritty political question—that is, whether or not to include food in the GST legislation. The GST is only part of the government's tax reform package. Would you please elaborate on your views on adding further complication to the GST by including or excluding food.

Mr Nenna—The point to make is that, from our perspective, and it brings to bear the initial comments I made, our members have to deal with the taxation system on a day-to-day basis. You referred to us as experts. One of the points I am making is that I do not know if there is any such thing in tax any longer. One of the issues in relation to exempting food for GST is that, inevitably, it will—and I mentioned this before—exponentially increase compliance costs. It will do so in two ways. It will introduce issues of delineation between what is exempt and what is not. We are confronted by that on a day-to-day basis under the current wholesales sales tax system that has essentially up to seven individual rates of tax.

There is fruitless litigation going on all the time in this country in relation to classification issues to do with the current sales tax law. In relation to overseas jurisdictions such as Canada and the UK that have multiple rated GSTs, the situation is similar there—that is, pointless litigation in relation to points of greyness, of classification, between what is exempt food and what is not exempt food and whatever other exemptions you wish to make. That is one element of it.

The other element of it is especially in relation to the point of retail sale. To the extent that you have a single rate, retailers relatively simply can accommodate their cash registers and point of sale equipment to apply a single rate of tax to a total on the tax invoice or the receipt. Once you have got different rates of tax, that ability is no longer there. The systems then need to interrogate the individual items on that cash register slip. With sophisticated point of sale systems, the system will have to identify the item code, then interrogate the database for the product and identify what tax code it is, and then apply it accordingly on the cash register. We are talking about tens of millions of dollars for large retailers to do that and proportionately so for smaller retailers. Our main concern is compliance costs as far as the exemption of food is concerned.

I do not want to pass on that question without reiterating the earlier point that I made. We do recognise that there is a legitimate argument and discussion to be had about the potential impacts on low income households and fixed income recipients of taxing food under the GST—that is, taxing food to the extent that it is not taxed already. We are not experts on this but from the evidence that we have been given, a more targeted approach to compensation would be much more efficient. It seems to us that simply excluding food will benefit those that it is not intended to benefit at the end of the day, and that is not economic.

Mr Drenth—I would like to make a couple of points on the numbers there, if I may. Before I do, on the classification issue that Mr Nenna mentioned, I spotted an article in the press last week about a UK classification dispute involving maggots, and the argument about whether they are a food. I suppose it depends on whether you are a fish or a fisherman, but that is an issue that is actually going to court.

In Australia, with the wholesale sales tax system, we have had endless disputes, the most recent one involving frozen yoghurt. There were three separate court hearings before the matter was finally resolved. There will be endless issues like that if we try to exempt food. The Treasury wrote to this committee last week saying that the estimated revenue impact in the year 2000-2001 for exempting food would run to $4.465 billion.

I went back to an article written by Geoff Lehmann, from the accounting firm Price Waterhouse Coopers, who looks at this question. He writes in the *Australian* most Fridays. He used information which shows the percentage spent on food from total income, looking at the poorest 20 per cent of households, the middle 40 per cent and the top 40 per cent. That shows, not surprisingly, that there is a higher propensity to consume income on food in lower income households. However, in terms of the total dollars spent, the information shows that the wealthiest 40 per cent spent nearly 50 per cent of the total expenditure on food.

If you translate those numbers to the $4.465 billion that Treasury told this committee about last week, exempting food is basically giving people that are well-off and some that are, on any objective basis, quite wealthy, a $4 billion free kick. Why would you want to do that? Our view is that, as Mr Nenna says, a more direct way of compensating people who need it is far preferable. Indeed, that is the way that Australian governments have generally approached equity issues.

Senator GIBSON—Thank you, Mr Drenth. Just taking up your last point, I refer you to a paper which Neil Warren, an associate professor of ATAX at the University of New South Wales, gave to this committee on 17 December entitled, *Food, staple of life or staple of GST?*. He has basically made the same point as that which you have just made. Going on from that, he also attached to the paper 30 pages on the definition of food from the UK legislation, just to illustrate the point that it is very complicated.

You made the point, Mr Nenna, about the pointless litigation which is going on. I remember someone coming to see me last year about tax and pointing out that the amount of litigation that is actually taking place in the UK on the definitional problems with the VAT is as large as the litigation on income and other taxes. Can you confirm that?

Mr Nenna—I have just come back from a review of the GST in Canada and the UK, and that was the experience conveyed to me by experts in that jurisdiction.

Senator GIBSON—In other words, if we do have further exclusions, such as food, we would really be giving a free kick to the lawyers.

Mr Nenna—That was my point in relation to the compliance costs associated with litigation. It is rife under the current wholesale sales tax system, so why would we be rejecting a system and then imposing a system that contains the same inherent problems? We are trying to improve the system; we are not trying to maintain the problems of the current system and have them perpetuated.

Senator MURRAY—If I understand you correctly, you argue against introducing differential rates of GST or zero rating, on the grounds that it introduces undue complexity and definitional problems; is that correct?

Mr Nenna—Yes.

Senator MURRAY—You are opposed therefore to the exemptions for education, health and financial services?

Mr Nenna—In broad principle, we probably would be. Again, one needs to take a balanced approach. There has to be a balance between the complexity that is involved in the multiple rates and exemptions, as against the gains that are purported to be made by undertaking those exemptions.

The next question to ask is this: is there a better way of achieving the objective that you sought by exempting financial services or exempting medical products? In relation to financial services, a lot of work is being done to see if there is another way of achieving the same result. There does not appear to be any practical solution in that particular instance, despite incredible amounts of research into ways of achieving the same result. I am saying that, in principle, a broad based single rate—the fewer exemptions, the better—is what we are proposing and what we would be in favour of. However, there are some instances where that may not be practically achievable.

Mr Drenth—But the senator makes a valid point. The government has decided to zero-rate certain items in relation to health and education; that is quite so. Some work has been done to help clarify where the boundaries are; and how that finishes up working in practice remains to be seen. We are saying in relation to food, Senator, that it opens up a Pandora's box which is far bigger, and that is going to add significantly to the overall compliance costs.

Senator MURRAY—But you do accept my point, don't you, that it is practically, theoretically and philosophically a position of integrity to argue for no exemptions, because you can justify that, or to argue that certain exemptions are possible but that, once you argue that some exemptions are possible, it is quite possible to add to those—which, indeed, already the Vos committee has done on education and health and which, as you know, the Democrats do on food? I want to leave it there. I am glad you gave me an honest response to that. My second question really relates to a fundamental issue: do your members trust politicians?

Mr Drenth—I have never asked them that question, Senator.

Senator MURRAY—I suggest you do so, because the Roy Morgan research indicates that the trust of politicians has fallen from 20 per cent in the 1970s to seven per cent currently. The reason compensation is attacked in the opinion surveys is that people do not trust politicians to leave the compensation in. As you know, in New Zealand they took it away. Why would you argue for a position where compensation should be substituted for exemptions, when the people do not trust politicians?

Mr Nenna—If you take that to its logical conclusion you could say that about any aspect of the tax reform proposal itself. How do we know whether food that is exempted will be taxed or whether items that are taxed will later be exempted? The same argument would apply in relation to, really, any aspect of this tax reform. What the parliament enacts, the parliament later can resile from, alter or amend. It is no different from the rate, the base or compensation. They are all in the same boat.

Senator MURRAY—Let me try a question on democracy, then. Democracy is founded on the will of the people. If between 60 and 70 per cent of the people do not want a GST on food, do you think it is appropriate for the government, therefore, to accept that, even when you might disagree with it?

Mr Drenth—If you ran the government by having a plebiscite on each and every issue, you may as well not bother to have a government. Governments are elected to make decisions. Another example might be the death penalty. Polls show consistently that there is a strong majority of people in favour of the death penalty, yet Australian states do not impose it and, presumably, politicians in those states have decided not to adopt that common view.

In relation to zero rating food and the trust that people may or may not have in politicians, it is a political problem and not one of tax design. I guess it is a problem that we would like to go away, but it will not go easily. It is clearly a concern that a lot of people have.

For what it is worth, I have read a view expressed that exempting food from the GST actually may create a moral hazard in that we will then already have exempted health, education and food and future governments might say, ‘Well, blow it, we will increase the rate because poor people are already protected. We have basically exempted all of the necessities of life.’ If you leave food in, you have still got to run that gauntlet. I do not know what sort of legs that argument has got, but it is an argument that needs to be considered.

Senator MURRAY—Let us move to the food issue. Fourteen out of 18 OECD countries that have a VAT or GST zero rate food or tax it differentially. So hundreds of millions of people have accepted that food can be differentiated. Why do you think 18 million Australians will not be able to cope with that?

Mr Drenth—People will cope with a badly designed system if they have to but, just because 14 out of 18 OECD countries have decided to adopt a system which we believe is inefficient and inappropriate, that does not mean Australia should do likewise.

I was visiting relatives in the Netherlands the year before last and I asked them how they were faring with the GST because, like other OECD countries, the Netherlands has a lower rate. These are not commercial accounting people, and they told me that it is not a problem at all. Yet when Mr Nenna goes around and talks to specialists whose job it is to install systems and look after the compliance issues, they tell him it is a nightmare. So most ordinary people will not notice these additional compliance problems and costs, which in some cases will be passed on to them as consumers.

Mr Nenna—Just to complete that answer: in no jurisdiction would you get a consensus view or any agreement whatsoever that the exemption of food and multiple rates is best practice in terms of administrative design. Quite often the exemption has been from a lack of commitment to explore alternatives right at the outset, the politics of the situation at the time, the convenience of following a poll, or whatever. You would have no person in those jurisdictions saying that exempting food or anything else from the system was best practice. They will all point to the New Zealand system in terms of a best practice design. To the extent that that creates some problem elsewhere, the issue is: is there a better way of dealing with that problem? That is what I think should be properly debated and looked at.

Senator MURRAY—That is why I raised the issue of trust. Do you understand that?

Mr Nenna—Yes, fair enough.

Senator MURRAY—I want to extrapolate on the chairman’s questions earlier and on Senator Ferguson’s response. This is just a comment, not a question. What I read behind the chairman’s question is this: if business groups are putting a proposition to government privately, which they are entitled to do, and the government rejects it, will they cop it sweet or will they then come to the Senate and say, ‘We lost with the government, will you fight for it?’ That is the simple choice we face, and I will leave it at that.

I have read both Ralph reports to date and I understand the direction in which business is going and, indeed, the government’s thinking, which is to lower the marginal tax rebate which corporations at present have to pay. My question really relates to a submission by the Shop Distributive and Allied Employees Association, who appeared earlier. In their submission they put the proposition that corporations should at least pay a minimum corporate tax rate. Do you believe that there should be a minimum corporate tax rate which all companies should be obliged to pay?

Mr Drenth—The United States has a system known as alternative minimum tax. I am not an expert on the US system, but my understanding is that that was introduced because of the extensive tax preferencing which is a feature of the US system, particularly in the gas and mining industries but also in many other industries. It was found that companies were reporting very large accounting profits and paying very little tax, year after year after year, by reason of these very substantial concessions.

As the Review of Business Taxation's international perspective paper shows, Australia's tax system is not one that can be characterised as having many generous concessions for business. The major one is the R&D provisions, which have been scaled back from 150 per cent to 125 per cent in relation to depreciation. The international perspective paper puts Australia in about the middle of the field, although it is probably a bit more generous than some other countries in relation to long-life assets. What I am getting to in a roundabout way is the conclusion that an alternative minimum tax system is not really appropriate for Australia because we do not have the extensive tax preferencing that some other jurisdictions do.

Senator MURRAY—I will put a question on notice because I am at the end of my time. The second Ralph report says that Australia—and it is an Arthur Andersen international survey, as you know, of the major tax systems in the OECD—and the United States together have the most complex tax systems of all. My question on notice to you is: will the ANTS package make our tax system more complex or significantly less so?

Mr Drenth—We will take that on notice, Senator.

Senator MURRAY—Thank you.

CHAIR—Senator Murray neatly explained one of the motives behind my line of questioning at the beginning. Perhaps I should explain the other. Having sat through the period in which we had high tariffs in Australia, I experienced industry associations lobbying government to reduce tariffs in the national interest for a more competitive economy and then members of the same delegation seeking private meetings immediately afterwards, saying to government ministers, 'But in our case, we want some special exemptions from that general rule,' which I take as a two-faced approach—do this to everyone else, but spare us the pain.

The essence of my question is: given the report that I have read, is there a private agenda by some in business for special concessions within the package that the government has put while telling the rest of us what is good for us and what we should have to swallow as far as their view of what the national interest might be?

Senator HARRADINE—Mr Nenna, in your introductory remarks you said that CTA is committed to overall tax reform. That of course includes the review of business taxation.

Mr Nenna—My comments in fact were primarily focused on the system of business taxation, and that was certainly what I was referring to.

Senator HARRADINE—And how is Ralph?

Mr Nenna—John Ralph personally, or his report? How is the report proceeding?

Senator HARRADINE—Yes.

Mr Nenna—It is proceeding reasonably on track. We have received the initial paper, which we have been very encouraged about—the foundations paper. The reason we were encouraged about that—and, again, I made this point in my earlier remarks—is that it was so appropriate before embarking upon specific proposals for reform to really look at the whole system in its proper context. As the paper espouses, the first thing really to look at is what are the national objectives and therefore where does tax fit in in terms of promulgating and promoting those particular objectives. So there is a debate to go on first and foremost before you get into prescriptive reforms as to what is the objective of the exercise at the end of the day.

Raising tax for raising taxes sake and increasing tax revenue may in fact be a very short-sighted approach to achieving what might be the ultimate objective. Raising an additional dollar of tax revenue in a particular situation may in fact cause a negative impact in relation to real economic growth in excess of the money collected. That has to be borne in mind. If raising a dollar of additional tax is cause for disinvestment, and that investment dollar was going to create more than one dollar of economic growth for the country and therefore tax dollars in the future, then that is not a proper and appropriate objective of tax. So that was one of the issues: to put the tax debate in its proper context and look at overall economic objectives.

The second aspect that gave us good cause for optimism is that it put on the agenda the issue of process—the process by which we have come to be in the situation we are at today, which is processes in relation to development of taxation policy, in relation to the process of legislating tax law and the processes of administering the tax law. To a certain extent, those have all happened in an ad hoc way. I think it is about time that people really sat back and looked at how we approach those particular aspects of the way the tax law has come to be developed. If there is a problem now, let us see to what extent those processes have been, to a certain extent, a contributing factor. Certainly, we have things to say about that.

We think that it was very incisive of Ralph to have put that squarely on the agenda up-front. Those are some positives. There have been extensive submissions on that initial paper, and we await the specific technical issues paper that is due later this month, as I am told.

Senator HARRADINE—Thank you, Mr Nenna. You were saying that the overall picture of tax reform in Australia includes the GST, marginal tax rates and other particular state-based measures—which I notice you mention in your submission—and, of course, the business tax. But the reason that I asked how the Ralph committee was going is because you are saying to us that you are supporting ANTS, the new taxation system.

Mr Nenna—I would not go as far as to say that we are supportive of the entire package. What I said, Senator, was that we support the initiative in ANTS that gave rise to an objective inquiry into the business tax system a la the Ralph committee. So we are supportive of the fact that the government through its ANTS package did set up a relatively independent inquiry to investigate objectively, through consultation and otherwise, the current business tax system. So we are supportive of the process.

There are some specific measures in ANTS itself in terms of business taxation that we would have some concerns about. I mentioned one of those in my opening remarks to do with entity taxation and in particular the deferred taxation proposals which we have got some concerns with. We are canvassing our members on other proposals within ANTS at the moment in relation to consolidated returns, for example, which sounds great. It has got certain appeal for our members and others, but it has got a number of complexities and difficulties associated with it as well. That needs to be investigated properly and properly debated. And there are other measures.

Senator HARRADINE—Yes, but shouldn't we, as members of parliament, have the benefit of what specific proposals will emerge from the Ralph committee? Should we not do that before we decide issues on other matters, for example, which are part of the context to which you are referring?

Mr Drenth—Senator, that is a question of the timetable that has been established for this committee and for the Ralph review. I understand this committee will be concluding its proceedings by about 19 April. The Ralph review is due to report by 30 June.

Senator HARRADINE—The government is expecting or hoping that the cement will be in place and solid and unchangeable in so far as its tax package is concerned as it relates to the GST and other aspects of the tax system but not in respect of business taxation.

Mr Nenna—I think that its approach, Senator—if I understand it correctly—is probably to subject the business taxation system to a proper inquiry, then come to a view as a government as to what proposals it wishes to go ahead with having taken account of all submissions. At that particular point in time, I would imagine that it would be open to the Senate to again review what the government is then intending to propose. I suppose the government would say it has the prerogative to examine the options and inquire as much as it needs to to determine its particular view in relation to whatever reforms it chooses to go ahead with or does not choose to go ahead with. It does not necessarily, as I see it, cut out an opportunity for Senate review.

I said this in relation to one of the dilemmas that we had. We are currently looking at what the options are. Our members are developing their own views as to the way some aspects of the business tax reform package should go ahead. But they are in the process of developing that for submissions to an independent inquiry which, I think, is a reasonable way to go.

Senator HARRADINE—If we are looking at tax reform as a whole, why shouldn't we be looking at business tax along with other taxes, such as broadly based consumption tax, income tax and so on? Why shouldn't we be looking at it as a whole? Why shouldn't we have everything on the table from the government as to its proposals in respect of all those matters before we make up our mind on any of them?

Mr Drenth—The proposed review of business taxation is quite clearly to be a revenue-neutral exercise, which is a fact that business is constantly reminded of when it raises particular issues. Can I suggest that the broad equity concerns that arise out of the review of business taxation are unlikely to be the sorts of concerns that the committee is looking at now in relation to a GST. The review of business taxation is very important to the business community. As Mr Nenna said at the outset, our members are at the sharp end of the tax system. We see this review not as a way of reducing our tax burden or just generally improving the financial outcomes for our companies, but simply as a way of clearing away a lot of the legislative deadwood that has accumulated over the years and coming up with some sensible approaches to tax design.

I might add that we were encouraged, prior to the election, to see the Australian Labor Party take up a number of the broad policy positions that were set out in ANTS. I am not a political expert. However, it would seem to me that the sorts of philosophical issues that might arise at a political level in relation to GST just should not be there for the business tax review because, one, it is revenue neutral and, two, one of the major parties has signed off on a number of the broad proposals.

Senator HARRADINE—You are talking about revenue neutral. Are you suggesting to us that the government will not bring forward legislation which will in fact not be revenue neutral and will have effects on those other aspects of the tax package which we are addressing at the present moment? At least it will affect the persons that are affected by the tax package which we are considering at the moment.

Mr Drenth—I understand the point you are making, Senator. You can imagine that this is not an easy process for the business community either because you have capital intensive industries, you have other industries, and not everybody wants the same outcomes. However, I say again that business is constantly reminded by the Ralph review, and I understand the Ralph review is constantly being reminded by Treasury, that this will be revenue neutral. So I cannot predict what measures the government is going to introduce. But if they are as good as their word, the measures we will see will, overall, be revenue neutral for business.

Senator HARRADINE—There are some proposals that have been made to the Ralph committee, in submissions which are on the Internet, with which I have considerable sympathy and with which a number of other colleagues would have considerable sympathy. If they are inherently good for business but may affect revenue in one way or the other, wouldn't they be supported, or shouldn't they be supported?

Mr Nenna—We would strongly agree with you. It is a constraint that is being imposed upon the review. We would like it to be otherwise; we would like it to be more open so that it can consider the matters on their merits. We have questioned the definition of revenue neutrality—whether it has to be revenue neutral on day one or whether you can look at a longer term perspective, with positive revenue in the longer term. Unfortunately, that is not the way the current government sees it, so we cannot add it to our earlier remarks.

Mr Drenth—On the proposal to tax trusts as companies, for instance, there is a concern that this will have a negative impact on publicly or widely held public trusts, which we believe act as an efficient savings and investment mechanism which does not present any threat to the revenue. If there were to be, say, a carve-out of those entities from the proposed regime, there would only be a minor timing effect on revenue collections. We would see that as a very useful modification to the ANTS proposal which would not be seriously impacting on the revenue.

Senator HARRADINE—I refer to the third-last paragraph of your submission. You state:

Compensation has to be adequate and has to be seen to be adequate. However, issues such as locking in the GST rate into the future and maintaining the long-term level of compensation are political issues—not issues of tax design.

I would have thought that they were essentially and irrevocably issues of tax design.

Mr Drenth—I guess it is the point I tried to make in response to Senator Murray's question. We believe it is a political question and that it will be a question of the will of the parliament and, ultimately, the will of the Australian people. Who knows what the public response will be to a government, any government, which jacked up the 10 per cent rate—assuming it is introduced and introduced at that rate—to, say, 12, 14 or 15 per cent? I would have thought there would be some considerable political risks associated with that, but then I am not a political expert.

Senator HARRADINE—But the revenue goes to the states—

Mr Drenth—Correct.

Senator HARRADINE—and to jack up the rate you need the approval of the states. The states will be up there supporting an increase, surely.

Mr Drenth—It is a rare state of affairs for every state government to be of the same political persuasion, Senator. My hunch would be that there would be some problems associated with pushing that through.

Senator CONROY—I remind you of the saying, 'Never come between a premier and a bucket of money.'

Mr Drenth—I would not like to.

Senator CONROY—Of any political persuasion.

CHAIR—Can I point out that we are running over time now. I apologise to the next witness. Senator Conroy.

Senator CONROY—Mr Drenth, you say in your submission that the tax system can only be viable in the long run where there is a perception that all sectors pay their fair share. Would you say that all sectors are paying their fair share at the moment?

Mr Drenth—It is hard to say that unequivocally. There are always criticisms being levelled—sometimes on the basis of reasonable information, sometimes not—about different sectors. The press has been running hot this last week about what Mr Nenna referred to as 'the big end of town controlling the tax agenda'. I have to say that if the big end of town has been running the tax agenda, it is doing a pretty awful job.

Looking at the other end of the spectrum, there were plenty of criticisms levelled at the so-called black economy, which is people doing jobs for cash, and there were various estimates made of the revenue impact of that. So I am not going to sit here and say that I am satisfied that every sector of the economy is paying its fair share. However, I do believe that we need a properly resourced, well-equipped Taxation Office to ensure that people do pay their fair share.

Senator CONROY—Which sectors are not paying their fair share?

Mr Drenth—I am telling you I have no idea. My involvement is with the large corporate sector. My strong feeling about the large corporate sector is that it is paying its fair share. Certainly, the broad evidence about that would tend to support that.

We have the RBT paper that was released not all that long ago which points out not only that Australia's corporate rate of 36 per cent is a lot higher than that of many of our competitors but that, in 1997, the proportion that corporate tax bears of all tax in Australia is exceeded only by that of the Netherlands. That is a broad number but, nevertheless, it indicates that we are up at the upper end of the spectrum.

Senator FERGUSON—What is the RBT paper?

Mr Drenth—The review of business taxation—the Ralph review. Secondly, the tax office itself, in a media release it issued in May last year, pointed out, from public information, that the rate of company tax collections over the last decade had risen at double the rate of the rest of the economy.

Thirdly, the Corporate Tax Association itself runs an annual survey of tax payments made by its members, which consistently shows that our members pay significant amounts of tax. It is always open for someone to say, 'Yes, but it is not enough and it should be more.' All I can do is highlight the broad numbers, which I would suggest are not indicative of a system where corporates are playing fast and loose with the tax rules and are only paying tax when they feel like it.

Senator CONROY—But you are here supporting change.

Mr Drenth—Absolutely.

Senator CONROY—Therefore, given what you said in your submission about sectors paying their fair share, you must believe that some sectors are not paying their fair share. Otherwise, why are you supporting change? If people are all paying their fair share, why are you supporting change?

Mr Drenth—Senator, perhaps in our submission I was anticipating the spate of articles that appeared in the press last week—well, I wasn't really, but these things do pop up on a regular basis.

Mr Nenna—Can I just add to that. As again I mentioned fleetingly in my opening remarks, one of the major concerns we have with the current tax system is its complexity—the complexity that we are burdened with at the moment, and increasingly so. I am sure you have read of the statistics of 120 pages in 1936, 7,000 pages now, and three-quarters of those have come up in the last five or six years.

Senator CONROY—How many pages of tax legislation is this? How many pages are coming out after this is passed?

Mr Nenna—The GST legislation will get rid of a plethora of other taxes, including the wholesale sales tax. So in terms of indirect taxation, if you take the sales tax, the FID and BAD duties, state stamp duties in every jurisdiction, we would be hoping for a substantial reduction in the indirect tax laws as well as a rationalisation of those laws.

In relation to the direct tax system and the business taxation system, that is an open question at the moment. But we are certainly going to be fighting very hard for a simplified and a reduced volume of tax law and much simpler and clearer tax laws. That is what we are on about and what we will be arguing very strongly for in the review.

Senator CONROY—You discussed a little earlier the number of rates that apply, saying that the smaller the number, the more efficient and better it would be. You are arguing for the smaller number of rates.

Mr Nenna—Yes.

Senator CONROY—It is possible to come up with close to 10 different rates that will apply under this package. Are you aware of that?

Mr Nenna—In relation to the GST itself?

Senator CONROY—In relation to this package and its impact.

Mr Nenna—I had not analysed it in that form.

Senator CONROY—You have zero for child care and things like that, the standard rate of 10 per cent, the input taxed sectors like domestic rents, which are going up by three per cent—

Mr Nenna—Yes.

Senator CONROY—It is not even possible to estimate yet what rate financial services are actually going to pay at the end of it. Then you have got luxury cars plus the additional tax on luxury cars, you have got wine plus the additional tax on wine, you have got division 87. Are you familiar with division 87? It is a beauty. It is to do with long-term accommodation in commercial residential premises.

Mr Nenna—Yes.

Senator CONROY—There are a couple of different rates in there. Tobacco will be under a new regime, and there will be double taxation on petrol. So when you start to add those things up, the simplicity you say you are supporting is as complex, compliance-wise, as the system you say is terrible.

Mr Nenna—Senator, we do not resile from our call for fewer rates and greater simplicity. To the extent that the multiple rates within the proposals, as you have indicated, are able to be ameliorated, we would support that reduction.

As I said, there is a balance required on some occasions. For example, in relation to the zero rating or exemption of medical supplies and services, to the extent that they can be clearly defined, delineated and exempted, they will not impact. An example would be limiting it to prescription drugs. To the extent that those lines are clear, unambiguous and confined to a limited area, potentially an argument may be made one way or the other. It really depends upon the circumstances. But as a broad principle, our view is that the fewer rates, the better the system and the lower the compliance costs.

Senator CONROY—I want to turn to your comments about your prescience when you wrote this article. Would it not be fair to say that there is a scepticism in the community about large corporations, that at least some of them do not pay their fair share of tax?

Mr Drenth—I would agree that that is probably a feeling that is common through the community.

Senator CONROY—The recent media reports suggest that senior Taxation Office personnel seemed convinced that at least some businesses are actually running the tax system to their own benefit. What is your view of that claim?

Mr Drenth—I think that is an absurd statement to make. I have to say that I am a little hesitant to comment on a secret internal tax office document that is heavily edited and that was obtained by a journalist under FOI. I have not seen it; I am not sure if any of the committee have seen it. Nevertheless, I accept that it exists somewhere because the journalist is very credible and the tax commissioner has commented on it.

Senator CONROY—Your submission states, at page 1:

> The corporate sector does not see the tax debate in the context of one group gaining an advantage at the expense of any other group.

As business has been driving the indirect tax agenda, why should people not think that this is a grab for money by corporate Australia?

Mr Drenth—There was a report in the *Financial Review* this morning about the level of share ownership in Australia, saying that well over 40 per cent of all adult Australians now own shares directly, 5.5 million of them. Many more own shares indirectly through their superannuation funds. The point we are merely trying to make is that there is no clear divide between large corporates on the one hand and the rest of the community. They are very much integrated. In a sense, everyone is a capitalist.

Senator CONROY—Going back to your statement that you do not see the tax debate in the context of one group gaining advantage at the expense of any other group, what are your feelings when 52 per cent of the tax cuts proposed as compensation go to the richest 20 per cent in the community?

Mr Drenth—Paul Kelly produced a little table in an article in the *Australian* on 22 August last year, headed 'Cracks in the foundation of welfare lobby attack'. It is a simple chart which shows the percentage of income tax paid now by the top 20 per cent as 57.2 per cent and their percentage of the $13 billion tax cuts as 52.2 per cent. So that is slightly less than their existing percentage. As to the percentages of income tax to be paid in July 2000, the 57.2 per cent goes up slightly, as you would expect, to 58.0 per cent. That is a 0.8 per cent increase in the proportion of tax paid by the higher quintile.

In any progressive tax system, if you start reducing the tax rates, people on higher incomes are going to receive larger cuts. The government, in ANTS, has set a limit of $75,000 as the point at which the top rate cuts in. In other words, the taxpayer earning $75,000 gets the same tax cut of about $4,400 as a corporate high flier on $275,000 or whatever. I just make the point that, in a progressive system, these are the outcomes you are going to get. You can try to achieve a different outcome by giving larger tax cuts to lower income people, but you will finish up with a huge bulge in your rates in the middle somewhere.

Senator CONROY—It is possible to design a way to pass on tax cuts that do not automatically benefit the rich.

Mr Drenth—Sure.

Senator CONROY—But my question to you was, 'Do you support 52 per cent of the tax cuts in this package going to the richest 20 per cent?'

Mr Drenth—On the basis that that richest 20 per cent presently pays 57.2 per cent of all tax, yes, I do.

Senator CONROY—They are not Treasury figures; they are Paul Kelly's figures.

Mr Nenna—Can I say that I do not think that Mr Drenth and I could have personal views on that particular issue. We certainly have not canvassed our membership on the distribution of the income tax cuts along those scales. It is not a particular focus of our membership beyond the view that the income tax system has to retain some incentive for people to work, to invest and to save. That is all we would say.

Senator CONROY—The complexity that you were talking about earlier—the expanding pages—isn't it a fact that one of the driving reasons for the complexity is the fact that corporate Australia continually seeks ways to avoid, legally, its tax, necessitating a legislative response to try to ensure corporate Australia pays its fair share of tax?

Mr Nenna—That would not be the way I would understand it at all. There are various—

Senator CONROY—Isn't that what a tax executive does?

Mr Nenna—No. There are various components to what a tax executive does. First and foremost, a tax executive is invested with a responsibility of ensuring that the corporation he represents complies with the tax laws of the country. In addition to that, there is a responsibility there that the company does not pay any additional tax to that which—

Senator CONROY—The Kerry Packer approach: do not pay $1 more than you have to.

Mr Nenna—There is a responsibility there that companies do not pay any more tax than they are legally required to. I would question, senators, whether you individually pay any more tax than you are legally required to. Given that particular point, I suppose that there are some members, as there are whether you are talking about individuals, small businesses or large businesses, who try to push to the edge what is legally due.

To that extent there are certain safeguards with regard to the large end of town. One is that, as public companies, we are under greater public scrutiny than most others. I think that that is generally a deterrent to so-called pushing the envelope because if we do there are repercussions. I would say that our boards of directors are also as a whole very mindful of their civic responsibilities and responsibilities to the community as well. Those are matters that are taken into account, in our experience, at the corporate public company level. Therefore, whilst there are extreme examples as in any sector of the community, I think, overall, corporate Australia is very compliant.

In relation to the voluminous tax changes, there are various reasons for that. One would have to ask in some instances whether they were necessary in the first place or whether they were properly designed and needed to be structured in the way they were. Thirdly, they represent, by and large, an enormous increase in the tax base of this country. Since 1985, I do not think that there is $1 that can be earned now that is not subject to tax.

On the other hand, there are huge black holes, as we refer to them, in relation to the deductions available to corporate Australia. With capital gains tax and the increasing definition of what is assessable income, virtually no dollar that we earn escapes the assessable income tax net. In large part, the increase in the volume of tax legislation is a policy decision by successive governments to increase that tax base.

CHAIR—Thank you, Mr Nenna. I am not aware of any other questions from the committee, so I thank the Corporate Tax Association of Australia Inc. for your submission and for answering the questions of the committee. Thank you.

[11.52 a.m.]

HILL, Mr David Welbourn, Research Officer, Australasian Railway Association

KIRK, Mr John Philip, Executive Director, Australasian Railway Association

WILLIAMS, Mr Bryan Paul, Manager Programs, Australasian Railway Association

CHAIR—Welcome. I apologise for my late call. We will take it out of the luncheon recess and start on time at 1.30 p.m.

Mr Kirk—Thank you particularly for the invitation and opportunity to be up here before this inquiry. I would like to make a few comments about who the Australasian Railway Association is and who we represent, before looking at some of the issues of concern in regard to the new tax system. The Australasian Railway Association, otherwise known as the ARA, is the peak industry body for the rail sector in Australia and New Zealand. The ARA is a unique association. It represents the interests of both private and government-owned rail operators, both freight and passenger, track owners, manufacturers of locomotives, rolling stock, signalling and communications equipment, other equipment suppliers, maintenance and construction companies, freight forwarders, investment banks, lawyers, service providers, consultants and the two major rail unions. The association was founded in 1994 and currently has a membership of 120.

Members of the association employ over 75,000 workers in virtually all parts of both Australia and New Zealand. The rail industry in Australia provides significant economic benefits to the country of around $7 billion per year. The association members are large exporters of goods and services and their rail expertise is widely recognised in the region as being of the highest quality. The Australian rail industry presently holds overseas contacts worth over $500 million primarily in Asia.

The majority of our members, 90 per cent, is in the private sector and have profitable enterprises trading in highly competitive domestic and international markets. The association is entirely funded by its members through membership fees.

With regard to tax reform, the rail industry generally supports the principle of tax reform. However, it is concerned about five main issues that, if implemented as proposed, would have a devastating effect on the viability of the rail industry. These five main points are as follows: the reduction in diesel fuel excise that continues to impose a road user charge on rail; the effect of the proposed GST on urban passenger services; the inequity of applying a GST on inbound tourist rail but exempting airlines; fringe benefit tax inequities between company cars and public transport; and, existing tax act impediments to rail infrastructure investment.

I would like to make some comments about the levelling of the playing field between road and rail. Whereas I do not want to make this a road versus rail issue, there are a couple of points I would like to make on this issue. We believe that the road lobby has told this inquiry that all it wants is a level playing field between road and rail. Not surprisingly, we the rail industry agree that a level playing field is absolutely vital to the future development of our economy. However, our idea of a level playing field is a policy environment based on an integrated transport strategy that includes equity in infrastructure funding as well as equity in taxation and access charges.

The road industry claimed that they are taxed 2½ times more than any other industry. This is a rather mischievous misquoting of a study that found that in fact the road transport industry is taxed 2½ times more than the industry average. The same study found that the rail industry is taxed two to three times more than road and that the differential is largely due to the mass distance charge based access charges that are paid by rail for using that rail infrastructure. To level the playing field, the heavily subsidised road transport operators must pay a mass distance charge to pay for the cost of road infrastructure, similar to that paid by rail.

The ARA understands that the government intended to level the playing field by reducing diesel fuel excise to 18c per litre for both rail and road. However, a study by a respected independent transport economist clearly shows that the reduction will benefit road transport more than rail, resulting in an undesirable modal shift from rail to road.

I will make some comments about this proposed reduction. Road transport requires three times more fuel for the same freight task than rail. Cheaper fuel will benefit road more than rail because the relative costs for road will be reduced more than those for rail. Modal shift of freight from rail to road will increase transport costs by increasing road construction and maintenance costs, fuel use and greenhouse gas emissions.

The proposed diesel fuel excise of 18c per litre is widely recognised by the National Road Transport Commission, the Bureau of Transport Economics, the National Farmers Federation and the Road Transport Forum as a road user charge. It cannot be a road user charge if it also applies to rail. Applying it to rail effectively removes two-thirds of present road user charges that are made up of fuel tax and registration. If the proposed 18c per litre diesel fuel excise is a common tax on rail and road fuel use and not a road user charge, then all users of diesel fuel must pay it and a road user charge for heavy vehicles must be introduced. Such does not exist at the moment. This charge must cover the cost of road use in the same way that rail pays an access fee for the use of the rail network.

Rail, unlike road, pays a genuine mass distance based track access fee. This typically comprises 20 to 30 per cent of rail operating costs. Without a user charge on fuel, road operators would only pay $458 in truck registration charges to move around 1,000 tonnes of freight from, for example, Melbourne to Sydney. By comparison, rail will pay $5,585 in track access fees to move the same 1,000 tonnes.

If the 18c per litre is a road user charge, then payment by rail is inequitable and discriminatory. All other off-road business users of diesel fuel, including marine business use, will qualify for a full credit of diesel fuel excise. As an off-road user, we believe rail should also be exempt.

I will make some comments on urban and commuter rail passenger fees. The new tax system will increase rail passenger fares by 10 per cent while simultaneously reducing the price of motor cars. In addition, businesses will be able to claim GST input tax credits on petrol for businesses using motor cars, saving around 7c per litre on current prices. The combination of these factors will be an increase in car use in urban areas at the expense of public transport. Australia already has very low public transport patronage. It is typically only one-third of that of European cities and is one of the lowest in the OECD countries. Increased public transport fares will also discriminate against low income earners reliant on public transport for accessibility.

Policies favouring motor cars over public transport contribute to the significant social and environmental cost of motor cars by increasing road demands, increasing air pollution and greenhouse gas emissions, increasing road accidents and increasing urban congestion.

Another area that we are concerned about is the inequities in fringe benefits tax on rail passenger fares. The new tax system, as we understand it, retains the existing anomaly of different rates of fringe benefits tax applying to employer provided cars and public transport fares.

At present the fringe benefit tax applying to motor cars as part of salary packages is approximately 10 per cent of the vehicle’s purchase price whereas the FBT applying to a public transport ticket is approximately 95 per cent of the ticket price. Lowering the FBT applying to public transport fares to the same level as that applying to cars will provide an incentive for companies to include public transport fares as part of salary packages.

The last point I would like to make in this opening preamble regards the impact of the GST on inbound rail tourist services. The new tax system proposes that overseas tourists who pre-purchase travel within Australia will be exempt from the GST if their domestic travel is by air. There will be no GST exemption for rail fares. This anomaly will severely affect rail’s competitiveness in the domestic tourism market. For example, a one-way first class ticket between Sydney and Perth on the *Indian Pacific*, one of the world’s great train journeys, will increase by a massive $126.

Imposing the GST on fares for long distance rail travel by inbound tourists when air travel in the same circumstances will be exempt from the GST will inevitably damage rail businesses servicing the tourism market in competition with airlines. I should also point out that a number of these services have recently been privatised.

In conclusion, the Australasian Railway Association supports integrated transport planning. We believe that, as proposed, the new tax system fails to achieve this because it is heavily weighted towards road transport with regard to both cars and trucks. More road transport will result in increased road wear and tear, increased road demand, increased fuel use, increased greenhouse gas emissions, increased urban air pollution and increased road congestion. These are all significant economic costs to the community that will increase the cost of transport. For these reasons the rail industry is seeking amendments to the new tax system.

CHAIR—Thank you, Mr Kirk, for—if I may say so—one of the more succinct submissions presented to us recently. Do any of your colleagues wish to supplement your remarks? I am not soliciting; I am asking.

Mr Hill—No, thank you.

Mr Williams—No, thank you.

Senator FERGUSON—I can understand why Senator Conroy did not want to be on this part of the inquiry, although he is still here because, as a former representative of the Transport Workers Union, he would have lots of things to say about road transport and other matters.

Mr Kirk, rail is definitely better off under this tax reform package, isn't it? Even though it might not give you all that you want, rail would be actually better off than they currently are with the package as it is?

Mr Kirk—Not with regard to the issues that we have outlined.

Senator FERGUSON—No, but in the overall tax package, if nothing was to change, you would not be as well off as you would be under the new tax package, would you?

Mr Kirk—I am not sure I could agree with that based on these major issues which we have all agreed are going to be very costly to the rail industry.

Senator FERGUSON—So you are saying publicly that in fact under this new tax package you will be worse off than you are under the existing system?

Mr Kirk—Yes, we are. Our costs will increase whereas our competitors' costs will decrease.

Senator FERGUSON—I am glad it is on the public record because, having looked at your submission and other information I have to hand, I would have thought that, taking everything into consideration with this package, the rail system is definitely better off, but we will leave this as a debate if you insist that it is not. Do you know what it costs to park a car in Melbourne today?

Mr Kirk—It varies. Earlybird parking is around $11; daily parking is about $18 a day.

Senator FERGUSON—Do you think that the actual cost of transport determines whether or not someone takes public transport or brings a car into Melbourne each day?

Mr Kirk—I think there are a number of issues that determine why people take public transport. It is to do with the cost of transport, the transit times, aspects of convenience and reliability. There are a number of complex factors why people use or do not use public transport.

Senator FERGUSON—There is the cost of parking, the cost of running a car and the cost of registering a car. Fortunately I live 100 miles out of a capital city. I drove in this morning but I cannot see why anybody would bring a car into Melbourne. I would have thought they would all use your rail and public transport.

Mr Kirk—That is true. Unfortunately in this city in many ways it is quicker to drive in by car than it is to travel by rail.

Senator FERGUSON—It is quicker?

Mr Kirk—That is simply the comparison of the investment in road and rail in some corridors.

Senator FERGUSON—I am surprised you say it is quicker to come in by car.

Mr Kirk—In some corridors; not every route.

Senator FERGUSON—The effective excise that is payable on diesel fuel under this package as used in rail transport will effectively be reduced from 43c a litre to 18c a litre, won't it?

Mr Kirk—Only in Tasmania. In other parts of the country, for rail, it will be reduced from 35c down to 18c.

Senator FERGUSON—You pay less now than other operators for diesel?

Mr Kirk—In Tasmania, rail pays the state levy; in other states, we do not. So the reduction for road transport is around 58 per cent; for rail, it is only 48 per cent. There is a bigger reduction in fuel excise for the road transport industry than for rail.

Senator FERGUSON—If we use your figure of 35c or 37c, then, in effect, the diesel fuel that is used in rail transport will be reduced, on those figures, by at least 17c or 18c a litre, won't it?

Mr Kirk—Indeed.

Senator FERGUSON—Rail are big users of diesel, aren't they?

Mr Kirk—We pay around $170 million per annum for fuel excise. We anticipate that that will be reduced by about half, with the reductions as proposed.

Senator FERGUSON—And you say that, in spite of that reduction in the cost of the fuel that will be used, under the package you will be worse off overall?

Mr Kirk—There are complex factors involved. It is not a matter of just saying that by reducing the fuel excise to both rail and road to the same amount, therefore you have levelled the playing field and we are going to be better off. In fact, the way it works is that the cost advantage that rail now enjoys because it is able to move volumes of freight will be reduced. What happens with what is proposed is that the new tax system in fact penalises the most efficient user of fuel, which is rail, because we are far more fuel efficient than road. So it is going to cost us in competitive terms rather than in real terms.

Senator FERGUSON—Do you accept the figures which have been published, and I am sure that you have heard of them, which show that costs to the rail industry will be reduced overall by 3.8 per cent? Is that a figure that you have heard and one that you would say is in the ball park?

Mr Kirk—We have heard that figure—and it varies between four and six per cent.

Senator FERGUSON—But it is not a figure that you would dispute, given that there could be a slight percentage point either way?

Mr Kirk—That is a figure that we have heard. We have not done any economic modelling on that to see whether that is in fact the case. That is something that has been put us.

Senator FERGUSON—You talk about the cost of everything going up by 10 per cent because of the introduction of the GST. Have you also seen figures that have been produced that suggest that the estimate of price rises throughout your industry is 5.8 per cent, not 10 per cent?

Mr Kirk—We have seen a number of these figures. The issues of concern are that the rail industry is being seen as a total sector and there are inputs in the equation which say that you take passenger rail and freight rail, urban passengers and country passengers, you throw the whole thing into the mix and you come with an average. In fact, the rail industry is comprised of a number of separate, discrete business sectors, and the tax system will affect those various sectors in different ways.

So you can bandy figures around saying the overall average will be such and such, but the inputs into that system are basically flawed. For example, we believe that those figures include, for diesel fuel excise, all the urban passenger systems in this country. Most of those passenger systems—probably 98 per cent of them—do not use fuel; they are all electrified. So the inputs into the equation are flawed.

Senator FERGUSON—Did you say you believe those figures are used or do you know those figures are used?

Mr Kirk—I said I understand those figures are being used. We have not been able to do any modelling to check them, but our understanding, when we asked questions about how those figures were arrived at, was that they did include all urban passenger systems in Australia, which of course do not use fuel.

Senator MURRAY—Mr Kirk, have you had the opportunity to read the Road Transport Forum's submission?

Mr Kirk—No, we have not.

Senator MURRAY—My summary of their submission is that they believe the new tax system will deliver them lower costs which can then be translated across to lower costs for all the people they service. My understanding of your submission, in summary, is a plea that your competitiveness with road is made fairer, more even. So there are two entirely different approaches. In the Road Transport Forum's discussion, they did not outline to us a competitive view with your industry. Is it your view that, over the past decade or more, road has been positively discriminated for and you have been positively discriminated against, when you look at the competitive nature of your two industries?

Mr Kirk—Indeed, I think that would be the case. If you look at infrastructure funding, it is quite clear that there has certainly been a considerable amount—something like 30 times—more federal funding for the national highway system than there has been for the interstate rail network.

Senator MURRAY—From memory, it is about $36 billion versus $1½ billion in the last decade.

Mr Kirk—That is correct, yes. In addition, we believe that since 1992, when the National Road Transport Commission introduced its new regime of charging, and also prior to that, when we have been paying fuel excise, there has been position. That has been endorsed by the Productivity Commission on a number of occasions, and by other inquiries, as well—that rail should not be paying that road user charge component of fuel excise. So we believe that has been discriminatory as well.

Senator MURRAY—If the low cost regime for road is advantageous to the country, wouldn't one option for you be that, rather than attack that as a system, you merely argue that you be given far better treatment within the tax package than you currently experience? So leave road with their advantages but actually radically increase your advantages. Do you have any propositions on that front to put to the committee, and have you any costings to provide to the committee of what that would mean?

Mr Kirk—The only position we have to put to the committee is that we believe that rail should be completely exempt from paying the fuel excise.

Senator MURRAY—Do you know what that would cost?

Mr Kirk—That would cost the government $85 million, which is around two per cent of the cost to government of $3½ billion for reducing fuel excise on overall transport. So it is a very small percentage of the overall cost to government. The studies done by the Productivity Commission in 1994 estimated that the reduction in fuel excise for rail would in fact lead to a productivity gain for the overall economy of $120 million, savings to farmers of around $40 million, savings to mining of around $20 million. So although there is a cost to government of $85 million, the benefits certainly outweigh the costs.

Senator MURRAY—Thank you. With regard to a second line of inquiry we had with the Road Transport Forum, there is the issue of differentially taxing clean versus dirty fuels, or relatively clean versus relatively dirty fuels. Surrounding that proposition is the issue of technology, whether the technology exists at present to commercially provide either LNG or LPG alternatives. Can you tell me if the technology yet exists for rail to use LPG or LNG and, if it does, would a differential excise rate encourage conversion to that?

Mr Hill—There have been trials in the United States with LNG which have been successful. The major problem is storage and conversion. Those trials are ongoing and there is no reason to suggest that in, say, 10 or 15 years that may not occur in Australia if these trials in America prove to be successful.

The problem with the present tax package, apart from rail paying the road user charge, is that by reducing the level of excise payable on diesel you are discriminating against investment or conversion to alternatives which, at present, have a cost advantage over diesel. Given that diesel is 25 per cent more greenhouse intensive than petrol and has lots of nasty emissions, including particulates which are carcinogenic, any encouragement of diesel fuel use in urban areas will only exacerbate existing urban air pollution problems. In view of those sorts of problems, reducing the level of excise on diesel goes against worldwide trends to increase the level of excise on diesel to discourage use of that fuel.

Senator MURRAY—Are you intending to make a submission to the environment committee, which is specifically looking at this area?

Mr Hill—We understood that our submission to the committee was overarching, that it went to all of those committees.

Senator MURRAY—This is the overarching committee. Nevertheless, the environment committee will specifically look at recommendations on fuel and the alternatives which could be considered in policy terms between dirtier fuels and cleaner fuels, and the incentives, the technologies and all the other issues that go with it. It is just a request from me that you consider a supplementary submission to your existing submission to go to them.

Mr Kirk—Thank you, Senator. We will take that on board.

Mr Hill—I would like to pick up on Senator Ferguson's line of questioning. The whole point is not so much whether rail's costs have been reduced. The fundamental issue here is: why is rail paying a road user charge? Rail's costs are being reduced—that is perfectly true. However, the fundamental issue that cannot be escaped is that there is a road user charge applying to rail, whereas no other off-road users will be paying it. That is the issue at stake here. As we have said, we are looking at a cost to rail operators that would be a cost to the government of $85 million compared with their forgoing of $3.5 billion. That is the primary issue here.

Senator MURRAY—My last question refers to the relationship between infrastructure and fuel costs. Would you agree, as a generalisation, that road infrastructure has been so heavily invested and is so materially advanced that the priority road gives to fuel costs is natural because that is the area of most immediate impact to them, whereas in your industry, with the underinvestment on infrastructure, an improvement in infrastructure spending would probably have far greater impact than the matters which arise out of the tax policy? In other words, tax policy is very critical to the road industry; but, in your case, the case you have been putting to Senate committees and in your lobbying for many years is that your greatest weakness is in the infrastructure area, and that is not something which can be dealt with in this tax policy.

Mr Kirk—I would agree with your summary to a point. It is absolutely true that our outdated infrastructure and the lack of investment in our infrastructure certainly has an impact on fuel use, and our competitors certainly benefit from improved infrastructure. However, the study that we have had undertaken recently indicates that, if the tax package goes ahead as planned, there will be a significant modal shift from rail to road in three main corridors: Melbourne to Adelaide, Melbourne to Sydney, Sydney to Brisbane. If that is the case, then basically it completely negates the case for investing in the infrastructure because there simply will not be rail running freight; it will all be on road.

Senator MURRAY—To summarise, your case is that that can be corrected by the government relatively cheaply.

Mr Kirk—That can be corrected for an $85 million cost to the government.

Mr Hill—If I can pick up on that point, the main issue in all of this is that fuel costs to truck operators are around 30 per cent of operating costs, and for rail they are about 20 per cent. Therefore, if you decrease the cost of fuel for trucks more than for rail, you are giving them a slight cost advantage over rail because they use three times as much fuel and therefore benefit far more from cheaper fuel.

The point we would like to make is that one train alone between, say, Melbourne and Sydney can replace 150 semitrailers and use about one-third as much fuel. So the question this committee has to ask itself is: do we want to discriminate against rail by retaining the 18c, diverting freight to road and putting a lot more semitrailers on the road, which in the end will lead to a greater call for federal road funding for increased road construction, maintenance costs and all the rest of it; or, for a simple fix of $85 million, do we keep a lot of that freight on rail?

Senator SHERRY—Is it correct to surmise your position as being that you accept that there is a small reduction in overall cost but it is at the cost of a significant competitive shift towards road transport, which you do not want?

Mr Kirk—Again, we are unsure of the accuracy of the benefits in that those figures are three to six per cent. We have been told by Treasury that that is what the benefit would be to us. Given the inputs that they have made into the equation, we have some considerable doubt about the accuracy of those figures. But it is correct that we believe that, if there is a benefit to be gained from the new tax system, it will certainly be negated by the fact that a large part of our industry simply will be non-viable, non-competitive, because it will—

Senator SHERRY—You just made the comment that you have considerable doubts about the cost reduction. In which areas do you have these doubts?

Mr Kirk—In the area of this quoted figure of between three and six per cent in overall cost reduction for the entire rail industry.

Senator SHERRY—Why do you doubt that?

Mr Kirk—As I mentioned in an answer to Senator Ferguson's question, the inputs are for all the rail sector, which is all urban, all country passenger, long distance passenger and freight, whereas in fact you would need to look at the impact of the tax package on each particular sector, since it will affect each sector quite differently because of the markets they operate in. The freight sector operates in a very competitive environment where the slightest trends in terms of the elasticities of the market will have dramatic effects, so things like price sensitivities, sensitivities regarding reliability, service quality and so on will see major shifts. We believe that the impact of the tax package with regard to the fuel excise will lead to such a modal shift, so we need to look at each of the sectors differently rather than as a total rail industry. The urban passenger sector, for example, which does not use fuel, is going to be affected in quite a different manner from the general freight industry.

Senator SHERRY—So, for example, passenger trains—forgive my ignorance; we do not have them in Tasmania—

Mr Kirk—You used to.

Senator SHERRY—Yes, I know. I took a ride on the last one from high school to the centre of Hobart city. It cost me 3c. Those were the days. That was 30 years ago. With electric passenger trains—I assume there are some in Melbourne and Sydney; I have never travelled on them—are the cost reductions likely to be greater in that area than, say, in the freight area?

Mr Kirk—In terms of the tax?

Senator SHERRY—Yes, in terms of the impact of the tax package.

Mr Hill—Our understanding from our urban rail members is that there will be very little cost reduction. In fact, if anything, they will have significant cost increases. Their cost of investment will go up 10 per cent; therefore, the recoupment period will increase proportionately. All the costs of their inputs will increase significantly; therefore, their call on government funding to supplement the difference in revenue versus cost will have to be increased, which will not be recouped by the 10 per cent on fares. It will go straight back into government revenue.

That is one of the other issues about the 10 per cent increase in public transport fares. It negates any ability of urban rail operators to increase fares for ordinary revenue producing purposes for investment or to reduce costs or whatever. So you not only have a 10 per cent increase in fares but a 10 per cent increase on inputs as well. As I say, the indications from our urban rail operators are that they will have very little benefit at all from this tax package.

That underlies what we were saying before: with the Treasury lumping all these things into an amorphous model with spurious assumptions, altogether you come up with a woolly number and who knows what it represents? It affects different sectors in different ways. Certainly, our urban rail operators will not be benefiting very much at all.

Senator SHERRY—So, in respect of passenger rail, they are going to get locked in a vicious cycle. If they try to put up prices, they lose passengers, they lose revenue, passengers will shift to, presumably, motor vehicles—

Mr Hill—Absolutely.

Mr Kirk—Which is going to be cheaper and fuel credits for business. And on it goes; it is a downward spiral.

CHAIR—How many people travel to work by train and go home by train in Australia, do you know?

Mr Hill—About 450 million use urban rail services throughout Australia each year. About three-quarters of those would be journeys to work.

CHAIR—You say 450 million trips?

Mr Hill—That is right, which keeps around 370 million car journeys off urban roads each year.

Senator SHERRY—And they face a cost increase?

Mr Hill—They face a cost increase of 10 per cent, automatically increasing fares which, as I say, will negate any ability by passenger rail operators to increase fares for any other purpose.

Senator SHERRY—It seems to me, reading your submission, which I compliment you on, that you cop it every way against all competitors.

Mr Hill—We do.

Senator SHERRY—Why do you believe you have received this treatment?

Mr Kirk—I would put it down to the fact that a lot of the accepted transport paradigms go unchallenged. People generally believe that we have to have an extensive road network, that we have got to spend billions of dollars on it, that it is in the best interest of our economy to do so. When we put these points, we are therefore always seen as an industry that is mendicant and complaining. What we are trying to do is to redress the balance and say, 'Rail has in fact undertaken significant reforms. We are now a viable, profitable industry.' We are trying, basically, to change the paradigms that people generally accept.

I might point out also that these paradigms are generally pretty well accepted by the community. We recently undertook a Newspoll study and you may be interested in some of the results, which clearly conflict with the general wisdom of transport bureaucrats and transport departments. We asked about a change in government policy so that freight currently moved by railways would be moved by heavy and longer trucks. We found that 80 per cent of the population disagreed with that proposal. As to whether more money should be spent on developing the freight rail industry in Australia, 91 per cent of the population thought that was a good idea. Around 90 per cent of the population agreed with the proposition that there should be more government commitment to the rail industry. I think the public generally believes that there should be a greater commitment to the rail industry and that the past neglect ought to be reversed.

Senator SHERRY—There has been considerable interest, certainly in the last few years, in the development of tourist rail facilities. You may be aware that in my home state of Tasmania there is to be built—it is not just a proposal—a world-class tourist railway, referred to as the ABT, with considerable public investment in the construction of that railway. Do you believe the—

CHAIR—There is one in Western Australia, might I say, already established.

Senator SHERRY—Okay. Coming back to Tasmania, where we will have the best in Australia, if not the world—

CHAIR—The Hotham Valley railway has won tourism awards.

Mr Kirk—We have already some world-class railways on the mainland.

Senator SHERRY—Do you see the changes that you have outlined in your submission, vis-a-vis diesel and the impact on tourist rail, as having any positive impact or helping in any way these developments of tourist railways? It seems to me that it is going to adversely impact on the development of tourism rail in Australia.

Mr Kirk—That is certainly the information we have been given by present tourism operators, that they are very concerned about the impact of the new tax system on their business. In fact, the conversations we have had with the tourism industry also support that view.

Mr Hill—I might add there that the tourism sector also will lose jobs, as will the rail industry, if this proposal goes through, and in regional and rural Australia thousands of jobs will be lost. You will have the closure of rural branch lines, the closure of rural rail services; tourism services, be they rail or otherwise, will also be adversely affected. So regional Australia will cop it quite badly. It will not just be the rail industry. All those people in the rail industry can be added to the post office, Telecom, schools, hospitals. To all the other thousands of people throughout Australia who have lost jobs in the last couple of years you can add thousands of rail jobs if this package goes through as proposed and the 18c remains on rail.

Senator GEORGE CAMPBELL—I have just a couple of questions. Have you done any analysis of what impact this shift from rail to road, in terms of costs, is likely to have on rural producers? There are parts of this country, obviously, where the only access that rural producers have got to market is by using rail. Others will be able, I presume, to transfer to road. Have you made any judgment on what the likely impact is going to be in those areas?

Mr Kirk—Our study was looking at mainly mainline freight on the interstate network, looking at a modal shift. But anecdotal evidence that we have been able to glean from rail operators who, particularly, move bulk grain products is that there will be a modal shift again from rail to road. Grain trucks are able to carry more tonnage now in South Australia, and very shortly they will be able to do so across the rest of Australia. If you combine the two effects and we see that modal shift occur, that is going to add costs to, particularly, local government—especially in repairing roads.

Senator GEORGE CAMPBELL—Is that going to create a disadvantage between rural producers that have no alternative but to use rail to shift their product, and those that can transfer to road?

Mr Kirk—At the moment there is competition between road and rail in the movement of agriculture products. It is suggested that that may change: if rail basically goes out of business, you will be left with a monopoly supplier in road.

Senator GEORGE CAMPBELL—Presumably most of the long-haul stuff goes by rail currently.

Mr Kirk—Most of the bulk does go by rail. However, there are a number of long-haul companies who provide services to primary producers. We would estimate that that would increase.

Senator GEORGE CAMPBELL—Have you done any analysis or any modelling on what the likely impact is going to be on your market share as a result of this differential?

Mr Hill—The study that we had done looking at National Rail's business, for example, suggested 10 or more per cent of National Rail's business going to road, which puts an extra two to 300 trucks a day on the road between Melbourne and Adelaide—about a 20 per cent increase on existing truck traffic. You are looking at a five to 10 per cent increase on existing truck traffic between Melbourne and Sydney and between Sydney and Brisbane. So you are looking at quite substantial shifts there, and 200 or 300 trucks a day makes a big difference when you are driving on the highway. We have had that analysis suggesting 10 to 20 per cent, depending on markets and a few other things.

Senator GEORGE CAMPBELL—What is the likely impact in the longer term on the rail infrastructure?

Mr Hill—For a start, it undermines significantly the federal government's proposed $250 million investment in interstate rail, because there will be fewer trains running. As you have got fewer trains running, your unit costs of running each additional train increase. Therefore, as increased costs pass through onto the remaining services, you then have a second-round effect that more business is lost to road. It is similar to the point that Senator Sherry just made about urban rail: as your costs go up and you lose business, whether it is passenger or freight, it ends up in a downward spiral. The indications we have had are that potentially it could lead to the total cessation of Melbourne to Adelaide rail freight services.

Senator GEORGE CAMPBELL—So, in fact, your argument is that over the long term this could, effectively, force rail out of business?

Mr Kirk—The study that we have had done, was done by a very respected economist who used to work for the road industry. Her study clearly indicates that there will be a dramatic shift, a dramatic effect on rail, if the proposal for fuel excise goes through as planned. The study is a cautious study. The actual effect could be actually higher than we have outlined, because of the competitive nature of the freight forwarding market that we operate in.

Mr Hill—I might add, just picking up on your previous comment about the cost to rural producers, that a couple of years ago when the western line to Adelaide was standardised from Melbourne it isolated some western grain lines. VicRoads, the road authority in Victoria, analysed the cost of sending all that grain by road, or converting the grain lines to standard gauge. They found that it was far cheaper to convert the grain lines to standard gauge for $30 million, and have all the grain go by rail, than it would have been to have heavier and more grain trucks running around that area. So that gives you a benchmark figure for the small cost on rail, as against all the other costs there would be on road.

CHAIR—I do not think there are any further questions from the committee. There is, perhaps, just one from me. Can you give us a cast-iron, blue-chip, ironclad, watertight guarantee that, if there are any cost reductions by virtue of this tax package, all of them, at 100 per cent, will be passed on and none of them will be held somewhere in the system?

Mr Kirk—I do not think anybody could give that guarantee. Certainly our indication is that our competitors are not making those guarantees.

CHAIR—I thank you for your attendance here today and for your submission, and for the way in which you have answered questions. The hearing is now adjourned for lunch.

Proceedings suspended from 12.34 p.m. to 1.36 p.m.

CHAIR—The committee will come to order. I will in a moment call Mr Steven Shepherd of VECCI. Before I do so, and if I may, I address this not to VECCI but to the wider audience that this inquiry has attracted. I wish to make a statement on behalf of the committee which is a unanimous view of the committee and the statement is self explanatory. Its heading is, 'Unauthorised disclosure of evidence and documents'. Senate Standing Order No. 37 provides that evidence taken by a Senate committee and documents presented to it which have not been reported to the Senate, shall not, unless authorised by the Senate or the committee, be disclosed to any person other than a member or officer of the committee.

Accordingly, in the course of this in all Senate inquiries, persons making submissions are advised that they may not disclose their submission to other persons until the committee has resolved to publish it. Such advice regarding the disclosure of submissions was reinforced by this select committee both in the initial press advertisements announcing the inquiry, and subsequently in acknowledgment letters sent to all parties making a submission to the inquiry.

Unauthorised release of inquiry submissions threatens the integrity of Senate inquiry processes and, as such, may constitute a contempt of the Senate. Parliament Privilege Resolution 6 specifically defines matters constituting a contempt to include unauthorised disclosure of evidence.

In December 1998, the Senate Committee of Privileges noted that culpability for unauthorised disclosure includes the recipients of improperly disclosed material and not simply the source of the information. In instances where the media is the recipient of improperly disclosed material the privileges committee noted that:

> . . . more often than not, it is not the content of a document which is of intrinsic interest to media recipients: rather its leaking makes the material newsworthy and frequently leads to biased or distorted reporting. The media, if they knowingly receive a leaked document or an improper briefing on committee proceedings, are complicit in any undue attempts to influence or distort the outcome of deliberations of a Committee. The Committee therefore warns media recipients of leaked information that, while it has in the past been reluctant to punish the media without satisfying itself as to the source of the information, it may not be so restrained in the future.

That is the end of the quote by the Senate Committee of Privileges.

The committee wishes to stress that parliamentary privilege exists for the purpose of enabling the Houses of Parliament to effectively carry out their functions. In accordance with this, unauthorised disclosure of committee documents can be expected to be examined by the Committee of Privileges on an assumption that a contempt is likely to be found.

To date the committee has resolved to release submissions as evidence is taken at public hearings. Indeed, today we have released all of the submissions of parties appearing before us today. The question of the wider release of submissions has yet to be decided by the committee. At this stage it is our intention to release submissions that relate to phase one of our inquiry at the time of our first report on 18 February 1999. I ask that that statement be noted.

[1.40 p.m.]

HRISTODOULIDIS, Mr Con, Senior Economist, Victorian Employers Chamber of Commerce and Industry

SHEPHERD, Mr Steven, Director, Policy and Communications, Victorian Employers Chamber of Commerce and Industry

WOJTKIW, Mr Steven Andrew, Manager, Economics and Research Services, Victorian Employers Chamber of Commerce and Industry

CHAIR—Having made that statement, let me turn to the witnesses before us from the Victorian Employers Chamber of Commerce and Industry. I welcome you and invite you to provide us with a brief overview of your position and to make yourselves available, if you will, for questions from the committee.

Before you proceed, it has been pointed out to me by the secretariat that you have provided a supplementary submission or a final submission which we did not cover in our authorised release this morning but I now ask formally that submission 122A be formally released. I note the agreement of the committee; it is thus formally released. With all of that now discharged, Mr Steven Shepherd.

Mr Shepherd—Thank you, Senator Cook. This afternoon, members of the committee, we intend briefly outlining VECCI's position on tax reform and how we see the GST ultimately rolling out. My colleague directly to my right, Steven Wojtkiw, is our manager of the economics and research services department and he will spend some time just looking at some of the industry and compliance cost issues associated with the new GST system. My colleague immediately to my left, Con Hristodoulidis, who is our senior economist, will specifically talk on some of the food and federal-state implications, as we see it.

Briefly, I thought it was worthwhile just spending one minute to make sure everyone understands who we are. VECCI is the largest multi-industry organisation in Victoria and, clearly, one of the largest in Australia. We have some 7,700 members. They cover the full spectrum of Victorian industry. We have around about 2,000 members in the manufacturing sector and the remaining close to 6,000 members effectively representing the broad structure of the services sector.

The majority of our members are small to medium enterprises. Something like 90 per cent of our members are SMEs. We provide a whole range of services and represent our members on a whole range of policy related matters.

Generally, in terms of VECCI's involvement, it is worthwhile just reiterating our involvement in the whole tax reform debate and, in the preliminary submission that I sent to the Senate, I outlined the various documents that we have put together on taxation reform. It is a fairly voluminous body of work—I think it was well over 1,000 pages. We believe we probably did two major pieces of work on GST.

The first really occurred in what we called the employers' tax plan which we released in 1990. In the employers' tax plan—I will not, obviously, go into all the details but just give you a feeling of where we have come from—we advocated a 15 per cent broad based valued added tax. In order to offset the introduction of that tax, we argued for the replacement of the wholesale sales tax system, appropriate compensation for social security recipients and about—at that stage—$10 billion of cuts to personal income tax. That was the first major piece of work that we did.

The second major piece of work was really in the lead-up to the combined ACCI ACOSS tax reform summit in late 1996. That document was called *The case for an efficient and equitable broad-based consumption tax*, and the key message that we attempted to articulate in that document—and we will go through the findings of that analysis in a bit more detail—is that we believe, in looking at the whole of tax reform, we found that the business and welfare groups were both talking about tax reform but using entirely different language.

Business groups were largely talking about the need for improved efficiency in terms of the operation of the Australian taxation system, whereas the welfare sector was largely talking about the need for improved equity in the operation of the tax system. We believed that you could potentially marry both concepts together. They were not mutually exclusive and we attempted to do that in looking at a more equitable GST type of package. I released that. That was one of the seminal papers released at the ACCI ACOSS tax reform summit back in 1996. We did send you a copy of that in terms of our original preliminary submission.

Just briefly: in that paper we looked, effectively, at three different alternative options for reform of the indirect tax base. Our preferred option was to have a 15 per cent broad based GST. I am sure you have had lots of different estimates of the size of the black economy. We believed there was something to be gained from the black economy, at a relatively conservative estimate of around $1 billion dollars per annum. We advocated the abolition of the wholesale sales tax system, the abolition of payroll taxes, a reduction in excises and an increase in social security benefits, and we made an estimate at that time that around $13.5 billion would be available for income tax relief. That was the sort of logic and rationale that we had done our analysis on.

In terms of trying to combine this issue of equity and efficiency, we estimated that there would be something of a fiscal dividend to be gained from the introduction of a GST type of system. We believed that fiscal dividend would manifest itself in two ways: firstly, there would be an increase from the black economy—the estimate that we had put together was around about $1 billion dollars in tax receipts per annum. We believed also that there would be some growth in just a general efficiency gain in the economy from having an abolition of distortionary taxes such as operated through the wholesale sales tax system, which tended to undermine the efficiency of industry. We estimated that it could potentially generate an additional $500 million per annum in revenue to the government. So, on the whole, we estimated there would be something like an additional $1.5 billion in taxation receipts which would emanate from this sort of tax mix switch.

As part of that, we argued at that time that there was a role for determining the overall size of the fiscal dividend—obviously, we have made an estimate prior to its introduction.

We suggested a range of key indicators would need to be developed, presumably by federal Treasury, so as to effectively measure the actual size of what that fiscal dividend might be. We suggested at the time that such indicators could involve an increase in business registrations beyond what is currently expected, such as the New Zealand example of greater than projected GST registrations. Also, indicators could involve estimates of likely revenue based on known registrations prior to the introduction of a consumption tax and the projections of anticipated tax revenues for a given level of GDP growth.

Assuming that there was some form of fiscal dividend which did actually materialise and was actually measurable, as evidenced by some sort of modelling work, statistics and key performance indicators that federal Treasury had put together, what would happen to that fiscal dividend? Would it just go directly to government coffers, to be expended appropriately? We said that there was an equity argument that at least 50 per cent of any particular fiscal dividend should be used to overcompensate low income groups. That was our strong recommendation at that time. So that goes beyond the normal social security compensation package.

Because we were very much mindful of the political environment and the equity issues pertaining to the introduction of a GST—which obviously very few people argue against on the basis of efficiency, but the arguments tend inevitably to come down to issues of equity—we did an analysis of the total income deciles across the Australian landscape. The focus of our analysis was on the three lowest income deciles. For example, we estimated there were something like two million households in the three lowest income deciles; 1.53 million reported government pensions and allowances as their principal source of income. The household expenditure survey showed that these benefits make up something like 96 per cent of the incomes of these households, on average. We argued that obviously you would need to compensate by raising the appropriate benefit rates to offset any potential loss that those low income earners could face who secured their source of income by that means.

We estimated also that there were another 150,000 households in the three lowest income deciles where wages were the principal source of income. Those households received something like 98 per cent of income from wages, and according to the household expenditure survey paid only $134 million in income tax. The cost of living for those households would rise, we believed, by about $360 million, and we argued at the time for a need to change income tax thresholds to effectively ameliorate the potential impact on those low income earners who used wages as the major source of income.

There were a remaining 270,000 households in the three lowest income deciles whose principal source of income was from either business or capital. Those households received some income by way of government benefits and paid $129 million in income tax. We believed the cost of living for those households would rise by around $536 million. However, we believed again that if income tax thresholds were adjusted to eliminate taxation of these incomes and if those households benefited from an increase in welfare benefits, there would remain a shortfall in compensation. But we believed that those households could effectively be compensated through some form of cash rebate paid monthly on the basis of the last income tax return.

So we did spend quite a bit of time, particularly in that paper of 1996, looking at how potentially GST might fall on those three lowest income groups, what their major current source of income was, what the potential inflationary effects would be of a GST and how you would structure the total compensation package in such as way as to ameliorate those effects.

There are just a couple of other comments I wanted to make. We are very supportive of the Small Business Consultative Committee, which the government has created. In fact, the chairwoman of our own VECCI small business policy committee, Dorothy Jellett, is a direct representative on that Small Business Consultative Committee.

The key issue that we would be arguing in terms of the government’s allocation of $500 million is that the bulk of those funds should be allocated to the new industries which, effectively, are going to be brought directly into the indirect tax net for the first time, ostensibly in the services sector. It should be borne in mind that manufacturing has for quite some time already laboured under a wholesale sales tax system, so we believe that where the additional cost compliance is going to fall is where those resources should be most adequately allocated. Also we support the approach of having different tax remittance payment periods, with the threshold of $20 million.

We have made a recent submission about the business tax reform committee. I could spend quite a bit of time on that; I will not but I might just make a couple of comments. One of the issues we looked at in terms of that work is a range of options for reforming the Australian business tax system between issues such as further cuts or changes to the indirect tax system as against changing the company rate of tax, as against increasing taxation expenditures as that affects the business community. One of the key areas we focused on in that analysis was its potential impact on the current account deficit. This was some modelling work that we had undertaken for us by the National Institute of Economic and Industry Research.

In comparing alternative options, it became obvious to us that it was preferable to reduce business indirect taxes rather than to reduce company taxes. We believe this may come about because companies in loss making situations clearly do not benefit from the company rate of tax cuts and obviously many small unincorporated businesses do not directly benefit from a cut directly in the company rate of tax. I could go on but I guess in the context of your deliberations some of those issues are not necessarily that relevant.

We are happy to take any further questions but now it is probably appropriate that I hand over to Steven Wojtkiw, who will spend just a bit of time looking at some of the compliance issues.

Mr Wojtkiw—Thank you very much, Senator and committee members. I reinforce Steven Shepherd’s comments that VECCI certainly appreciates the opportunity given to it today to present to this committee, given the announcement of the government’s tax package in August of last year. Some time has since passed. That time has been a particularly important one for VECCI and its members, not just in examining the legislation and specifics outlined in the tax package but also in ascertaining and examining the reaction of business members to the tax package and how they believe, from a practical point of view, they will cope in a new tax environment, come the year 2000.

Certainly more questions than answers have arisen amongst the briefings that we have provided over the last six months to members across many different industries, both service and goods producing industries and also regional as well as metropolitan based businesses, small, medium and large—VECCI's membership covers the diverse spectrum of Victorian industry. That being said, there has been overwhelmingly positive support amongst most members, if not all of them, for the reforms that are outlined, at least on paper at this stage, relating to the tax reform package.

There has certainly been a great degree of frustration on the part of business over past decades, as you would appreciate, with lags and only ad hoc approaches to tax reform from a holistic perspective. We are certainly pleased and our members certainly seem to be more encouraged by the particular scope and breadth of the reform that has been proposed by the government.

Having said that, there are some question marks, as I say, particularly relating to business compliance with the transition to a GST. I will just outline where those concerns are, and they are more concerns relating to information and education. It is quite pleasing that the government and its bodies are moving in the direction at this stage of helping to allay some of those concerns.

Certainly Steven has mentioned the allocation of $500 million to assist small- and medium-sized enterprises with improving their IT and record keeping requirements. In the transition to a GST that is going to be very important. We do not question in this particular forum the amount of money that has been allocated, but we do wish to stress that it is important, as Steven has announced, that the money is allocated to small- and medium-sized firms who do have the greatest compliance burden, whether they be in service industries or in goods producing industries.

Members do have concerns as to how they will in fact access those funds; the criteria for meeting that particular accessibility; the form of assistance—whether it will be in a rebateable form or some form of up-front cash payment. Certainly the issues that are arising there are those which we acknowledge do fall within the role of the small business consultative committee. We do believe also that this current Senate inquiry has a role and some responsibility to, if you like, put some form of pressure and momentum on those other forms of inquiry and the various subcommittees that do exist, both attached to this particular committee of inquiry as well as to others which the government has announced.

Definitional issues, many of which are to be examined by the tax consultative committee, still do attach themselves to definitions such as commercial and non-commercial activities and whether they are those relating to charities and non-profit organisations or more broadly across industry. There are obviously concerns amongst businesses as to understanding whether the activities they are engaged in are purely commercial, fully or partially commercial or, for that matter, non-commercial. That particularly affects business in the charitable and non-profit sector and also elements of government or semi-government bodies which have now found themselves in a corporatised process.

Therefore, we have issues as to the precise range and scope of services or goods to be taxed, and whether that is in financial services, medical, health or the education sector is still yet largely to be clarified. As to issues such as what are in fact zero rated goods or services and what particular items of business input may well receive input tax credits, they are certainly issues that VECCI is endeavouring to work through with its members to help provide a greater degree of clarity on those particular questions.

What it does indicate to us from the feedback from our various briefings and committees that we engage ourselves in regularly with business members is that there is a greater role for education and improved information as to the tax reform proposals which are before us. Certainly the ATO, through its web site and other mediums, have provided an increasing array of fact sheets which have been used with greater coverage amongst businesses. VECCI also, as do other business groups, have a particularly important role at this stage in helping to disseminate much of that information.

Finally, if you certainly are in business, as many of our members are, there is a degree of scepticism still attached to the role of the Australian Competition and Consumer Commission in monitoring wholesale and retail prices in the transition period to a GST to ensure that price falls emanating from cuts in indirect taxes, and particularly sales tax, are passed on not just to consumers but to all producers along the supply chain.

They are, perhaps, very simplistic but nevertheless important perceptions and feedback which we have received from many of our businesses, which I am sure you will receive from other witnesses before this particular inquiry, but I would like to leave you with some of those sentiments and views which we have certainly found to be the most pressing ones amongst our members.

CHAIR—Thank you. Mr Hristodoulidis.

Mr Hristodoulidis—I would like to add just a couple of issues. One deals with food as that was part of your terms of reference, and the other issue is federal and state relations because we did a bit of work on that last year.

With food, it gets back to the issue that Steven Shepherd talked about earlier. We think that people get mixed up between equity and efficiency in the debate about food. On the one hand you hear some people argue that if food is excluded from the GST base that the government has proposed there will be a loss of revenue, and they go through the efficiency arguments. On the other hand you have other groups who say that food needs to be exempt for equity purposes to compensate low income households.

In terms of a preferred approach, VECCI takes the debate apart and says that if food is to be excluded from a GST base for equity purposes and for compensation packages our approach would be as outlined in the paper, as Steven said—that is, do it through the social welfare system through some sort of increased compensation or welfare payment, and even maybe through some sort of voucher system in terms of food expenditure for low income households.

Generally speaking, we think that a tax system needs to be simple with a minimum amount of holes. If you start excluding things like the Canadian government did when they introduced their value added tax system you get a loss of confidence in both the political system and the political parties involved in the political system.

In terms of federal-state financial relations, we also welcome the changes the government has produced by passing the goods and services tax through to the states. Last year we consulted Professor Neville Norman from the University of Melbourne to undertake some work for us on Commonwealth-state financial relations in trying to alleviate some of the vertical fiscal imbalance that exists in the system. His estimates showed that a GST of around 10 to 12 per cent would raise enough revenue to abolish the wholesale sales tax system, the payroll tax and the FID and BAD systems the state governments impose at the moment. Obviously, that is a little bit different to what the federal government has recommended at this stage in terms of the goods and services system where they abolish more stamp duty based taxes rather than the payroll tax system.

The central point where we support the government is that a goods and services tax that provides revenue to the state governments is one tax rather than nine other tax systems. It is for that reason it is our preferred approach to go down that route rather than have state governments oppose narrowly based and differently based tax systems. At this stage I will leave it open to you to ask some questions.

CHAIR—I am sure you will not be disappointed. I will ask Senator Ferguson to ask some questions in a moment, but I will ask one question to begin with. The government has carried through the House of Representatives its legislation to give effect to the tax changes that it is proposing to make. Does VECCI support that legislation with respect to every provision of it or does VECCI harbour reservations about some parts of that legislation?

Mr Shepherd—VECCI's position is one of support for the government's general position. Our focus has been more about potential reforms or proposed reforms to other aspects of the Australian business tax system, proposals mooted around reforms to capital gains tax, FBT, et cetera. In the context of the general GST package, we are generally supportive of what the government has outlined, yes.

CHAIR—That is general. If I might be particular, do I take that to mean that you support every clause, subclause, placitum, section of all of the bills that have been produced and that you have no reservation about any of them?

Mr Shepherd—We do not have any substantive reservations. You can always argue with things like the development of thresholds at $20 million. Is that an appropriate threshold in terms of different tax remittance payment periods? Could you debate that the threshold should be higher or lower, et cetera? They are the sorts of issues that we could raise, but the reality is we have no substantive concerns at this stage.

CHAIR—Do you intend to raise with the government any changes at all to that legislation?

Mr Shepherd—To that legislation, at this stage, no.

Senator FERGUSON—My colleagues on my right in questioning an earlier witness talked about compliance costs. When I say on my right, Senator Campbell is usually on my left. Sorry, Senator Campbell.

With the issue of compliance costs, is it fair to say that the proposed system in Australia is more like the New Zealand system than any other goods and services taxes that are in other countries in the world as far as its nature and its breadth? I notice that in your report you talk about compliance costs where the average collection costs for the GST in New Zealand are around 1.1c per dollar revenue, comparing favourably with overall average cost of tax collection of around 1.4c per dollar revenue as with other systems. Firstly, is it a fact that ours is nearer to the New Zealand system than any other in the world and is it a fact that compliance costs have actually come down in their experience?

Mr Shepherd—I would argue, from a philosophical perspective, that the central reason the compliance cost would be lower associated with a GST system than, say, with what currently exists under the existing Australian taxation system is the complexity that exists with taxes like the wholesale sales tax system: is this item in or out of the net? The cost associated with getting appropriate accounting and legal advice to ascertain that is what really increases that compliance cost burden. That is the central reason, from a small business perspective, that we have argued for as broad and as neutral a GST system, if you like, as possible in order to minimise those potential compliance costs. That is what you are finding in that sort of analysis. That is the reason for that differential.

Senator FERGUSON—Have you got any idea how much would be added to the compliance costs if there were to be an exemption for food?

Mr Shepherd—We have not done a detailed analysis of that. Clearly there would be an increase in the overall compliance cost. It would be noticeable. Would it be overwhelming? That really depends. Those industries that are in or around what may or may not be defined as the food sector would obviously find an additional compliance cost that would not occur in other sectors of the economy because of the equal treatment under a GST system. There clearly would be a higher cost for those companies. In some ways, they may actually be penalised trying to ascertain whether this commodity is food or is not food.

There is one issue I want to go into more detail on. We have done a lot of research on the fringe benefits tax system, and there is the same concept with GST. What really annoys small business in particular is not necessarily the statutory rate of tax they pay. What really gets them is the compliance cost burden attached to meeting their statutory tax obligations. You would not believe it, and we would never lobby on it, but I have had small businesses say to me, 'I would rather have a higher company rate of tax, or I would rather a higher general rate of tax, if we had one tax and there was no compliance cost.' That is the mind-set. From a small business perspective—bearing in mind that that covers the majority of our constituents—that is what we are strongly advocating to the government at the moment.

Senator FERGUSON—In questioning one of the witnesses this morning, Senator Murray talked about the fact that there are exemptions or lower rates for food in 14 out of 18 of the OECD countries. We also have to bear in mind that they have a GST rate of between 15 and 25 per cent on other goods, which helps to compensate for the fact that there is none, or a lower rate, on food. I think it is important to take that into the equation. If we were then to include other necessities of life, as has been requested by some people in relation to the tax package, have you got any idea how much more it would add to the compliance cost if we keep adding exemptions?

Mr Shepherd—Obviously it becomes something of a exponential effect in terms of the overall compliance cost: the more items, the more commodities you attempt to exempt from the impact of the GST, then the compliance costs are going to keep escalating at each stage.

On the question about those countries that have exemptions for food, an interesting issue would be whether there had been an increase—and I am sure there is no evidence whatsoever to support this—or it had partly contributed to some sort of increase in the level of income inequality. I would strongly argue that there has been no impact in terms of increasing income inequality because you have had an exemption for food and the perception is that food represents a high proportion of the normal budget of a low income earner, therefore it is going to—

Senator CONROY—It is not a perception, Mr Shepherd. That is a fact.

Senator FERGUSON—Maybe Senator Conroy can ask his questions afterwards, Senator Cook, and let Mr Shepherd continue.

Mr Shepherd—We would argue, for those reasons, that there should not be exemptions. We just strongly believe that clearly, as evidenced by our own research, you are going to get an additional compliance cost burden once you exempt food. That compliance cost burden will accelerate once you start exempting other things.

Mr Hristodoulidis—In our submission we talked about the New Zealand experience and the Canadian experience. The Canadian government actually treated the tax on food differently for restaurants as opposed to food sold in grocery stores and we show estimates of the impact that had in terms of consumption patterns for different industry sectors. That is just one example. If you create that type of loophole in the system, that could occur in the Australian system. Where do you draw the line? Do we exclude all food items, or do we exclude food items in terms of necessities such as fruit, vegetables, milk and bread? You then get into the problem of manufacturers and wholesalers having to classify their products in the appropriate area.

Senator FERGUSON—If you are talking about fresh fruit and vegetables, we had the St Vincent de Paul people telling us the other day how the price of fresh fruit and vegetables had increased by 29 per cent in the past 12 months. But the Australian Bureau of Statistics tells us that only about $2 in every $100 of the household food budget—2.2 per cent—is spent on fresh fruit and vegetables, so there can be some distortions as well.

Mr Shepherd—Exactly.

Senator MURRAY—Mr Shepherd, large numbers of your members are Victorians and large numbers are in retail and wholesale businesses. Is that correct?

Mr Shepherd—That is right.

Senator MURRAY—I am told that the introduction of the casino in Victoria and the much greater extent of gambling that has resulted has damaged retail and wholesale business turnovers in Victoria. Is that correct?

Mr Shepherd—There is a time factor involved if we are going to get into a discussion about the effect of the casino on the Melbourne business community. Our general perception of that issue is that initially what happened was that there was clearly a level of competition between the casino and other businesses and there was a loss of business away from other businesses, particularly in the vicinity of the casino.

However, our perception now is that rather than be necessarily in competition with businesses, there has been an element which is more complementary to those businesses. Why? It is because we have seen much greater growth in Melbourne through interstate and international tourism and the level of expenditure that has been undertaken in Melbourne. There has been a downstream benefit to businesses associated with the casino. So, initially, there was clearly a competition effect where businesses were feeling the effects but we do not believe that is necessarily the case now.

Senator MURRAY—As I understand it, the effect of the ANTS package is to lower gambling taxes overall. What is your attitude to that from the point of view of your members?

Mr Shepherd—Obviously, gambling taxes have caused a significant increase in general revenue. Looking at it from a state revenue perspective, they have reduced, or at least in part alleviated, some of the taxation burdens that have been placed on the rest of Victorian industry. From that perspective we have been generally supportive of the increased reliance that the Victorian state government has had on increased gambling tax revenue receipts. So, generally we have been supportive of that increased reliance.

Senator MURRAY—I did not understand your response. Does that mean you do support lower gambling taxes or you do not support lower gambling taxes?

Mr Shepherd—Our general principle is that we support an increased reliance on gambling tax revenue but—there is always a caveat—the question is in what other areas of potential reform occurs. Obviously, from our perspective, if we are looking at it from a revenue raising perspective, if we have a situation where the Victorian state government increases the level of revenue from gambling taxes and that is offset by, say, a reduction in the payroll tax rate or a changing in the payroll tax free threshold, that is a change that we would support.

Senator MURRAY—Correct me if I am wrong, but I think your submission states that the automatic consequence of the introduction of a GST is that that GST will increase in later years. Regardless of what the ANTS package says, is it your expectation that the GST will increase in line with international experience? Why?

Mr Shepherd—We can debate this, but we believe that the reliance on direct tax revenues as against indirect tax revenues has been inappropriate. When you compare it to the OECD average, using that average as a benchmark—

Senator CONROY—What are those figures?

Mr Shepherd—I have not got the figures in front of me but we have put them in previous submissions. There has been a relative difference between our reliance on indirect tax revenue as against direct tax revenue. If you believe that, then we would argue that over the long term there is probably a rationale for actually increasing the GST rate—not that we are supportive of that. But we could understand it if the reliance on increasing the GST rate was done on the basis that it was changing the structure of total tax revenues and reducing the reliance on direct tax revenues. On the whole, we would be supportive of that. But, obviously, if it was being used simply to increase the total level of tax take and there was no reform in the direct tax system, then we would not be supportive of that move.

Senator MURRAY—You are familiar with the consumer household cameos that the Treasurer has put out in this package and the issue of compensation for each of those cameos and for large identifiable groups such as pensioners and self-funded retirees and so on. The inference behind that is that compensation will need to vary according to the economic circumstances of the groups or individuals concerned. If we accept that as a principle for households, I want you to consider it as a principle for businesses.

Earlier today, Senator Conroy gave a very useful summary of more than a dozen differential rates of tax which arise from this package as it is presently presented. These occur where industries are exempt, with some being GST free; where different rates of tax apply for petrol and excise and so on; with housing and accommodation—all that sort of thing. It adds up to well over a dozen. So it is a GST which will be introduced with a wide variety of rates. The question of compliance then arises. Are you familiar with the Walpole Evans study from the University of New South Wales? It is a useful study into the whole issue of compliance costs in these areas. From memory—and with that qualification—I think they indicated that the compliance costs will be about $1 billion for big business and about $9 billion for small business.

The point of my question is this: if you take a pharmacy which, under the government's projections, will have a range of items which are GST free and a range of items on which GST will be paid, the complexity for that person in dealing with their tax return is greater than for somebody for which it is all GST or GST across. Is it your belief that the government should consider compensation packages for businesses whose complexity of compliance is greater than others? Should they vary the compensation for such business types versus other business types?

Mr Shepherd—Yes, sure. In fact, I alluded to that in my initial presentation. Taking where we are at currently in compliance cost burdens across different businesses and different industry sectors—not that we are saying that is an optimum, just taking it as a given for a moment—we would be arguing that, where those businesses or industries are going to face the greatest additional compliance cost burden as part of this package, the $500 million in funds should be allocated to those businesses.

That might be to pharmacies, for the very reasons you have outlined, associated with the complexities of which goods are either in or outside the net, or to service companies, which clearly have not been directly in the indirect tax net—they never had to incur the wholesale sales tax system, for example. We believe the compensation package should be allocated to those businesses or industries which are going to face the greatest burden from what exists today. So I am basically agreeing with the sentiments of your comments.

Senator MURRAY—This is my last question. You would be aware of the issue under consideration by this committee as to whether food should be included or not included in the GST. You have made the point that making food GST free increases the complexity and compliance costs for business.

There are two ways in which you could deal with such an issue, were it to be considered by the government. One way is to define food very narrowly so that, in any given supermarket, fewer items are GST free and more items have GST on them. The other way is to define it very broadly. It is the issue of definition.

If this committee were to have to respond to the food issue and if, hypothetically, your organisation were to face a situation where food, or some items of food, were to be GST free, would it be better for your members—and perhaps you could say why—for there to be a narrow definition or a very broad definition? Which is the easier for you to deal with?

Mr Shepherd—Given that we have come from a philosophical position about the need to minimise exemptions from a compliance cost perspective, just looking at that perspective alone, and assuming you adopted that approach, I guess we would be arguing in the context of how you would structure 'food' if you were to make food GST free. We would be arguing for a narrow definition of what constitutes food, with fewer commodities within the basket of what now is constituted to be GST free. Therefore, with regard to additional compliance cost burdens across industries who are either in or around that sector of the economy, there would be minimum levels of disruption in terms of trying to ascertain whether their good was in or outside the net. So we would be arguing, from that broad philosophical perspective, that we would support as narrow a definition as possible, rather than a broad definition, if food is going to be made GST free.

Senator MURRAY—I said the last question was my last, but this is the last one. Have you surveyed your members to establish whether they want food GST free or not?

Mr Shepherd—In terms of surveying members specifically on food, no. Most of our research and surveying of our members has been on the general issue of taxation reform and issues. But certainly the common theme that continually comes through from members—and I am sure my colleagues will add to this—probably more anecdotally than in hard empirical research, has been, firstly, the need for broad based tax reform which involves the minimum number of distortions. Issues pertaining to the compliance cost burdens associated with things like the wholesale sales tax system for, obviously, that sector of the economy that is directly within the wholesales sales tax net really bug them big-time. The evidence that we get is for having the minimum number of exemptions possible, to minimise those distortions to keep compliance costs at a minimum.

CHAIR—I was just going to call Senator Conroy, but let me just ask you two quick questions. First of all, in your presentation, Mr Shepherd, I think you said you started the paper trail around about 1993 as to how you as an organisation began to work up your position on tax change.

Mr Shepherd—In 1990.

CHAIR—Should I understand that position to be one in which you favoured a goods and services consumption tax based as broadly as possible? You are nodding so I take that as yes.

Mr Shepherd—That is right. We did. If I could just comment on that: our constituency base has something like about 80 per cent of our members in the services sector. For an organisation like ourselves to go out on a limb potentially, which is obviously bringing those companies into the indirect tax net for the first time—and we have continued to advocate this and had support from our members and our executive council, which is our supreme policy making body—indicates that there is a reasonable level of support for this direction within our own constituency.

CHAIR—Support for the broadest possible base?

Mr Shepherd—That is right.

CHAIR—You have not got that, because the government has made major exceptions to its tax base in education and in health, hasn't it?

Mr Shepherd—That is right. Perhaps I could just cover that. While we advocated that, from looking at analyses of GST systems operating around the world we acknowledge that there are a couple of areas which really jump out at you in terms of problems in trying to impose a GST. Obviously, financial services is one: how do you define value added in the financial services sector? There are also issues pertaining to some of the problems associated with health and education. So I would retract my original statement—in our original document of 1990 we did actually say that areas like financial services, health and education should be outside the GST system.

CHAIR—So while you support the government legislation that is currently before the parliament, it is not the ideal legislation that you want, is it?

Mr Shepherd—The legislation that we have before us we believe is pretty much there. While it might not deliver 100 per cent of everything we may want, in terms of the real world realities of what we can get we think it is pretty much on the ball.

CHAIR—This is a question Senator Murray may ask: why do you drawn the line at education and health and not include food? That is not a question for me—it is probably an Australian Democrat question—but why do you make that distinction?

Mr Shepherd—In terms at looking at those sorts of sectors, when we looked at the operation when we started our original research, back in 1990, we looked at the introduction of GST systems right across the world. We identified areas where, for a whole range of political, administrative and other reasons, a GST was very difficult to actually estimate. As I said, an obvious one was financial services. My understanding is that no country today has actually introduced a GST on financial services, because of some of those definitional issues. It was for those sorts of reasons we put those issues outside the net.

CHAIR—But it is an arbitrary line that is drawn, isn't it?

Mr Shepherd—Sure.

CHAIR—And that means that anyone can decide, in the arbitrariness of that line, where it is more appropriately drawn?

Mr Shepherd—Yes, but the issue in doing that—and I keep coming back to the obvious difficult one, financial services—is that you have to make some fairly heroic assumptions about how you are going to define the base for GST tax purposes.

CHAIR—It strikes me as logical nonsense, if I may say so, that compliance costs grow exponentially as you exclude more areas from the package. Obviously, areas excluded do not have compliance costs; they have the compliance cost burden removed from them. The issue becomes definitional at the margin only. Can you justify to me the statement that it is exponential rather than simply linear?

Mr Shepherd—I guess the key issue is in terms of how the tax intersects with different sections of the business community, particularly the small business community. If the tax interacts in such a way, or the way the tax system is designed, that it results in the compliance cost burden around that particular definition capturing more and more small businesses, that is exponential.

I say that simply on the fact that we know, on all the best research—the work done by people like Jeff Pope at the University of Western Australia—that there are economies of scale in tax collections and that the impact of compliance cost for, say, the fringe benefits tax system was estimated to be about 24 cents in the dollar for a large business, while FBT compliance placed a cost burden of something like 46 cents in the dollar on a small business. So, if you have a situation where you are capturing a greater and greater proportion of small business in terms of trying to ascertain whether this commodity is either in or outside the net, then obviously there will be that sort of effect as small business is brought into it.

CHAIR—That is supporting the argument that the more you excuse from the net, the more you remove from compliance costs, and therefore the compliance cost as a feature of the whole reduces. Let me go to one last question. I took you to say, Mr Wojtkiw, that most members of your organisation were in favour of the package but not all. I made a note of that when you said it. What are the objections that those in your organisation who are not in favour of the tax package raise to your organisation?

Mr Wojtkiw—Perceptions are important—I think that holds in all levels of life. What we have found in going out on the hustings, if you like, and presenting the elements of the tax reform package to businesses, is that there has always been, particularly in the earlier part of the initial launch or release of the government's tax package, a great deal of confusion and uncertainty, because we are talking about change and change is always unsettling.

Businesses were perhaps not as fully aware or as appreciative of their compliance burden as they should have been, and they were not as aware or as appreciative of hidden taxes, which inevitably cascade on their business and their industry, that currently exist with the current tax system. So it is a matter of getting their minds around, firstly, what they are currently facing in terms of the tax system, and its impact on their business, and, secondly, and importantly, getting their minds around a fairly revolutionary, if you like, dramatic and fundamental reform of the tax system.

That is fairly difficult for most people, and businesses are no different. That is why we have found at least initial concerns arising from some businesses and some industries, but we have found that that is particularly related to greater education and information as to how they will be affected. That is the challenge that rests with business groups. It rests with government and its agencies and it certainly rests even with committees and inquiries such as the one being held at the moment in this particular forum. So it is more of perception than reality.

CHAIR—With respect, it sounds as though you are saying that the more you can educate your members, the more agreeable they will be to this proposition. What particular issues do those members who dissent from it raise to justify their disagreement with your support for the package?

Mr Wojtkiw—Aside from the educative issues and the information issues—and as you say, it is up to businesses to be informed and then to make decisions about whether they do or do not support particular tax systems and not for VECCI to make those decisions necessarily—there are clearly industries that are going to be winners and losers, or in a relatively better or a very much unchanged position perhaps. Examples do come to mind. We have undertaken some analyses of our own looking at specific industries. In manufacturing—for example, the tobacco industry—you would certainly find fewer benefits attached to the tax reform package because the government will maintain various excises and duties on tobacco products without repealing them as it will with other industries which have a large number of indirect taxes attached to them. For health reasons, perhaps, there could be arguments raised as to the efficacy of those decisions, but that is the path the government has gone down.

Similarly, the alcoholic or beverages industry perhaps would not enjoy the substantial benefits attached to the tax reform proposals because the government will maintain various levels of excise on, for example, wine products. So there are going to be business or industry groups which will not so much be losers but which will not enjoy the benefits of indirect tax reform as much as other industries. But, having said that, feedback from both our members and our own analysis shows that, on the whole, there are certainly more winners than losers in moving down the path of tax reform than what we have with the current system.

CHAIR—The examples you have given me are of two areas: tobacco and beverages. Is that exhaustive of those groups of your members that have objections to the tax package or are there others?

Mr Wojtkiw—There may well be others but they are the two which certainly came most clearly to mind when we were dealing with businesses through various briefings and other forums. So we are not discounting that there may well be other industries that have concerns. But, on the whole, through our reasonably extensive consultations, we believe there are fairly minor negative effects as it affects industry. We believe that the negative effects are really quarantined to industries such as the two that I have given you examples of.

Senator CONROY—You mentioned earlier that your members were concerned about the monitoring of the passing on of the cost savings. Would you view the Treasury assumption of 100 per cent of the pass through as a real world assumption?

Mr Shepherd—In terms of the analysis that we have undertaken, I cannot really give you a definitive answer to that. The real issue that we were alluding to earlier from an equity perspective is how should those funds ultimately be utilised. We argued from a broader policy and philosophical perspective there could be an argument, once you have fully measured what the benefits are likely to be, that that be used for strong equity bases and used to, effectively, even overcompensate low income earners. But that is the only analysis we have done.

Senator CONROY—I think maybe we misunderstood each other. I took it to mean, earlier in your presentation, that your members were concerned that the pass-through effects of the wholesale sales tax being abolished were not going to flow through to your members. Sorry, we probably misunderstood each other there. I was wondering if you could expand on that.

Mr Wojtkiw—It really gets back once again to businesses getting a good grip, if you like, on understanding their own cost structures that exist within their own firm and not least in the industry because, with the tax reform package, businesses need to be very clear about what their expense base is, what their expenditures are on inputs to their production or service outputs. It is getting an understanding of those expenses and the costs attached to those that is important if the business is going to provide or seek to lodge an input tax credit with the authorities. So they need certainly to be aware of what are the inputs and the true costs of those inputs. In ascertaining the true costs of those particular inputs, over time, with the abolition of indirect taxes such as sales tax, businesses then will have an expectation that many inputs will in fact be cheaper. They themselves are sourcing those inputs from other allied firms and industries, whether up or downstream, so there is certainly a very large and very real expectation that inputs to business will be lower.

The sentiment that I was expressing was certainly more that we look forward to having those lower costs and overheads passed on. We believe, in looking at our books and in looking at the activities and the prices and costs of supplies from allied industries, we will get across those issues as a business community. It is just a matter of whether all will play fairly in industry and in fact pass that on. That does suggest that, yes, there is a very clear and important role for watchdogs like the ACCC.

Mr Shepherd—And obviously the potential effect there is going to be different with different industry sections. Where there is a high level of concentration of power in a particular industry sector the potential for passing on may be quite different from another industry sector where there is a conglomeration of smaller players where they do not have the potential to demonstrate market power. So, obviously, they are the sorts of issues that we will be focussing on that the ACCC should be really concentrating on.

Senator SHERRY—So you do not believe there will be full pass on to all industries?

Mr Shepherd—I think it will vary. Generally, I think we have moved into a much more competitive environment, given that so many industries—as we have seen from our own surveys of our own members—have become much more export oriented, even small to medium enterprises who would not have been in export markets 10 years ago. So, clearly, the whole pressure in terms of becoming competitive—competing with imports, competing on exports markets—is much more prevalent. But I think there are different industry sectors which potentially give rise to different levels of market power. You may suspect that in those industry sectors the potential that that may not happen to the full extent is more likely than in other industries. Whether it does or not, I cannot say. But you would expect that there might be some risks.

Senator SHERRY—You suspect.

Mr Shepherd—There could be a risk, sure.

Senator CONROY—Will your members fully pass on cost savings?

Mr Shepherd—Absolutely.

Senator CONROY—As to the question of compliance, is Bob Beaumont with your organisation?

Mr Shepherd—Yes, that is right.

Senator CONROY—Mr Beaumont is quoted in the *Business Review Weekly*. His quote reads:

While large companies and fast-growing companies will be ready for it, most self-employed and micro-businesses still don’t understand it and some in the retail and wholesale sector will go out of business because of it.

Do you agree with Mr Beaumont?

Mr Shepherd—No, I think those comments have been an overstatement. Certainly, in terms of our own research, he works in a separate area which has basically been an independent company operating and associated with VECCI—a Business Angels initiative. He is looking at it from the perspective of dealing with small businesses really at the venture capital end of the market. He may have gleaned that perspective.

Certainly, in terms of our own research and anecdotal work, we believe that clearly there will be an additional adjustment for many small businesses in the services sector. But I do not think we have ever seen any information given to us by companies saying that this potentially means the death knell of their business. Certainly we have never had any direct evidence of that at all.

Senator CONROY—Given what you said a moment ago about fully passing through the cost savings, in your submission you refer to the benefit from exports of zero rating eliminating many existing taxes which impede the competitiveness of Australian exports. If all the cost savings that are coming from those abolitions are passing through, what is the benefit to your members? If all those savings that you are saying are happening and are, as you just said, passed through, where is the benefit to your members? I see benefit to your customers, but where is the benefit to your members?

Mr Wojtkiw—Members in terms of VECCI's business constituents?

Senator CONROY—Yes.

Mr Wojtkiw—Those businesses who are members who are engaged in export activity will themselves benefit through, I am hopeful, greater returns. That in turn should provide them with greater cash flow and that can only turn into opportunities for new investment and new job creation. So benefits to members would not be exclusive and they will not be definite. But, once again, businesses in those industries—and exports are the example we are talking of here—would stand to gain for the reasons we have outlined in our submission from the tax reform packages that we are talking about.

Senator CONROY—Can you quantify those benefits?

Mr Wojtkiw—We have not as yet surveyed businesses to quantify the gains but certainly that would be an area we would look at in the very near term.

Mr Hristodoulidis—It is difficult to quantify something you do not have in concrete. How do you survey your members when you do not know what the GST rate is and you do not know what the GST base is and businesses do not know what the implication is on their cost structure?

Senator CONROY—Are you aware that most of the modelling, even modelling that has been commissioned by Treasury, and independent modelling, has all argued that there will be an appreciation of the dollar which will wipe out the purported gains from this abolition of all wholesale sales taxes? In fact, some of the Treasury officials in papers have even described it as an illusion that exporters will benefit.

Mr Hristodoulidis—The modelling on the exchange rate, as I understand it, is not conclusive in terms of completely wiping out the benefits in terms of the lower costs, in terms of the appreciation of the dollar. As I understand it, there are some models that say there will be full parity in terms of the exchange rate and cost structure and other models that actually do say that there will be some sort of benefit that, in terms of the appreciation, will not completely offset any cost cuts. Again, it depends what model you look at.

Senator SHERRY—But there is a big question mark against these alleged benefits, isn't there?

Mr Hristodoulidis—Depending on which model you look at and think is correct.

Senator CONROY—The Prime Minister has publicly said this is a $10 billion benefit to business that is going to lead to more jobs.

Mr Hristodoulidis—You are talking again in terms of the exchange rate at an industry or macro level. If you look at each specific business itself, from when they had the pass through come through in terms of the wholesale sales tax, the FIDs, BADs and all the other stamp duties that are to be abolished, if they look at their individual cost structure and they are able to offer a competitive price on the world market, then you do not think that is going to have too much of an impact in terms of the dollar because that is one trade amongst a billion trades.

Mr Wojtkiw—The point my colleague is making is also one that price is not the only determinant of competitiveness. In that context, businesses facing a more streamlined environment, if you like, in terms of giving them the greater ability to get on and do what they do best—which is to do business, to develop new products, to develop new markets, new and innovative ways of packaging—

Senator CONROY—I am trying to find where that boost is coming from. You are passing on the full benefit in the non-export side right through to your customers so there is no benefit to your businesses. In the export sector the argument is about some modelling that says maybe no benefit, maybe a bit of benefit. I am looking for the $10 billion boost to jobs that the Prime Minister told everybody before the election we were getting.

Mr Hristodoulidis—We do have members who are exporters. In terms of that membership part of our base there is a direct benefit. Then, if you believe the argument that the appreciation does not completely wipe out the cost benefits, you are given those guidelines.

Senator CONROY—You said if the depreciation does not—

Mr Hristodoulidis—As I said previously, if you take one individual case, if you find one individual firm that does have the pass through in terms of their cost base and it goes down, you would not think that that one transaction in amongst billions of transactions would appreciate the dollar that greatly.

Mr Shepherd—But the real economic benefits, surely, come from what economists tend to call 'allocative efficiency.' If you do away with a tax system that taxes a whole range of different commodities at different rates, a system that clearly distorts resource allocation, and if you have one tax rate which taxes right across the economy, then resources are allocated to different sectors of the economy in terms of their real resource efficiency and are not based on some post-tax differential. That is where you get the 0.5 percentage point growth in GDP that we have estimated.

Senator CONROY—I am glad you have raised the allocative question. A number of studies, including studies that you may have seen that were put to this committee before Christmas, made a substantial amount of that issue. It was argued very strongly that our traditional exports, which are probably what your members would cover, have been declining in value over quite some time and that non-traditional exports, for instance, the tourism sector, is an increasing value good. However, the allocative effect of the tax shift is to push resources into a sector with declining returns and out of a sector with increasing returns. In actual fact, the potential job losses that will occur because of that shift in allocation is anything up to 100,000 jobs.

Mr Hristodoulidis—All our exports are zero rated so it does not matter. They will get the input tax credit so it should not impact on their cost structure. If you are comparing a manufacturing plant that exports versus an international tourist operator, they are both exports regardless of what type of service or good they offer. There is a 100 per cent pass through in terms of input tax credits for both the manufacturer and the international service provider in terms of tourism. I cannot see where your argument goes.

Senator CONROY—The study is arguing that because it is a more highly labour intensive sector, that having resources moving out of it, as Mr Shepherd has just described, there will be a greater fall in the jobs in the tourism sector than there is potential increase in, say, your sector.

Mr Shepherd—You have assumed that on the whole if you are comparing rates of return and levels of efficiency in tourism, which may incur an additional tax burden and does not exist now, as against, say, the manufacturing sector—

Senator SHERRY—It does incur.

Mr Shepherd—where it does occur, then what you have assumed is that the tourism sector per se is more profitable than the manufacturing sector per se. Clearly, pockets of tourism will be a lot less efficient, a lot less profitable, than different sections of manufacturing. So while on the whole you are right, when you look at the different industries which will be impacted through these changes that will clearly be different. While you can make a generalisation about tourism as against manufacturing, when you look at the specific mechanics of how it will operate, it will clearly be different.

Senator CONROY—I wanted to come back to the Prime Minister's comment about the $10 billion job boost. Are you familiar with that comment?

Mr Shepherd—Yes.

Senator CONROY—Would you sign up to that? Is it a $10 billion boost?

Mr Shepherd—In terms of the analysis that we have undertaken, and this is documented in the work that we did three years ago, we estimated that it would increase nominal GDP by about $2.5 billion and it would increase the cash economy by about $1 billion. So the sorts of figures that we have tended to run with have been on an annual increase of around $3.5 billion. This was based on some economic modelling done for us by Tasman Research.

You could use 10 different models and come up with different numbers but, put it this way, the general outcome was a positive addition to GDP, not a contraction, and that is the bottom line.

Senator CONROY—And over time? You mentioned earlier the 0.5 per cent increase in GDP. That was over how many years?

Mr Shepherd—That was an annual figure.

Senator CONROY—An annual figure?

Mr Shepherd—Yes.

Senator CONROY—Half a per cent extra GDP growth annually?

Mr Shepherd—Yes.

Senator CONROY—And that was from your model of three years ago that was totally broadly based, and with no exemptions?

Mr Shepherd—Pretty much, yes.

Mr Hristodoulidis—It had the exemptions of health and education.

Senator CONROY—I am just trying to work out how comparable that model is, as compared to this model.

Mr Shepherd—That is right.

Senator SHERRY—What does that mean in terms of jobs?

Mr Shepherd—I have not done the figures in terms of jobs, but to calculate it you would simply take total nominal GDP, which is about $500 billion, and divide it by the total value of wages, salaries and supplements in the economy. That is about $150 billion. So if there is about a three to one ratio then we would be talking about an order of that sort of magnitude. But, obviously, we have not done that analysis based on employment.

Senator HARRADINE—Dotted through your submission are references to New Zealand. If my memory serves me correctly, one welfare agency that came before us indicated that their colleagues in New Zealand found that after the GST settled down there some time after 1986, there was a significantly greater demand on their services by low income families and low income individuals for food and financial services and so on. Could you comment please on that?

Mr Shepherd—I guess that is a political decision that the government of the day has to make, but it does not necessarily mean that those changes are axiomatic with the introduction of a GST. That is a separate issue in terms of what a government may do in terms of the provision of the effective social security net.

A government could introduce a GST and introduce effective compensation for low income earners through the social security system, and over time erode that system so that the net position of those low income groups is to become more vulnerable and more exposed and actually result in a redistribution of income, if you like, against that sector of the economy. But that is a separate decision from the introduction of a GST. It is not axiomatic that by introducing a GST that will necessarily happen. That is a philosophical decision the government of the day will make.

Senator HARRADINE—You have seen ANTS. In ANTS, do you feel that the provisions therein, in respect of this question of erosion, are adequate to prevent erosion of the compensation?

Mr Shepherd—We believe that the compensation package—and it is not that dissimilar to the sort of work that we documented three years ago—is not that dissimilar. It provides an appropriate compensation package. I had this debate at the tax reform summit with academics. You can always find one individual, based on their level of expenditure, who is going potentially to be worse off. You cannot construct a tax reform package of this type that ensures 100 per cent of people are better off. That is obviously illogical. But we believe the compensation package is adequate.

The only thing that we would ask—and we have argued this with the welfare sector, I guess from a more philosophical perspective—is that where there are additional proceeds which accrue to the government from increased tax revenues over and above what has been estimated because of the black economy and any economic efficiency dividend, is what to do with those proceeds. We would say that there is some argument to actually over-compensate low income groups and those most exposed by using some of the proceeds—we have argued 50 per cent of the proceeds—to compensate them.

In order to do that you have to introduce appropriate measures about what the additional gain to revenue will be. If you do not do that then obviously this goes directly into government coffers and the government of the day will make decisions about how it allocates its overall taxation expenditure priorities.

Senator HARRADINE—From all of that, do I take it that you are not entirely satisfied with the provisions in the legislation going to the question of erosion of those compensation benefits?

Mr Shepherd—In the short term we believe that the compensation package is adequate on the whole. You can always debate individual issues but we believe the compensation package as it has been presented by the government is quite adequate.

Senator HARRADINE—In your submission you mention that in polls taken after the introduction of the GST in New Zealand in 1986 there was found to be strong support for a GST. Would you be good enough to lead us in the direction of when those polls were taken, when the last poll was taken and what were the results? These are not absolutely necessarily relevant to be quite frank but you made your point there and I would just be interested in the basis for that comment.

Mr Shepherd—I guess we can bring that material back to this committee at a later date. Obviously we are dredging up ancient history to a certain extent. This was based on work we did in 1990. We would have to go through all our papers to try and identify all the surveys that were taken. We got a lot of that information from New Zealand Treasury. New Zealand Treasury would have access to a lot of those surveys by the government of the day. I think it would probably be more efficient to go directly through the New Zealand government.

CHAIR—You may make it available through Mr Rob Diamond, the secretary of the committee.

Senator HARRADINE—If there were more recent polls in relation to those matters, I would be grateful for them.

Mr Shepherd—We have not really followed the more contemporary debate.

Senator GIBSON—Firstly, in following up Senator Conroy's questions to you about business costs being lowered, is it not a fact that the Treasury estimate in answer is that total business costs are going to go down by 3.2 per cent and that transport costs are going to go down by 6.7 per cent? You may be interested to know that last week the Road Transport Forum in evidence before this committee suggested that road transport costs for their sector—the large end of road transport—are going to go down by something between 15 and 19 per cent. Would you confirm those numbers?

Mr Shepherd—Certainly in terms of the general work we have done; we have done one-off case studies over time. I guess we have been involved in this debate for at least a decade. We have identified those sorts of cost savings. Obviously it varies by industry sector depending upon how they currently interface with things like the wholesale sales tax system, excises et cetera. But, yes, it can be as significant as that and the general estimate of around three per cent is the sort of view we are getting as well.

Senator GIBSON—May I move then to the definition of products and goods in classification for sales tax? You mentioned earlier on in your evidence that there was a lot of controversy now over compliance costs with business because of difficulty of definition between one good and another good around the boundaries of the seven classifications of wholesale sales tax. Let us say food was to be considered for exclusion from the GST. Again, we had evidence back in December given to us with copies of the definitions of food from the UK legislation which went to many pages and illustrated the difficulties. We have had people, including an earlier witness today, tell us that litigation on the definition of classification in both Canada and the UK is currently very heavy because of this very problem. Have you any comment to make on this classification and litigation problem?

Mr Shepherd—Obviously, again we just have a philosophical perspective. One way of minimising those potential litigation issues and potential costs is by having as broad a base as possible to minimise the issues pertaining to what is or what is not within a particular base. Our perspective would be that, with a broad based GST, issues pertaining to litigation associated to definitional issues would be a lot less than what exists at the moment because of the wholesale sales tax system about whether edible undies are classified as food or clothing, which I always like to quote as case studies. We think we could get away from some of those costs.

CHAIR—What is the answer to that question?

Mr Shepherd—Statutory incidence are first use so therefore they are defined as clothing rather than food.

CHAIR—I think perhaps we should cease to explore this line much further. Senator O'Chee.

Senator O'CHEE—Following on from that issue of what is food, it can be much more mundane than that, can't it? Say you are selling fatted lamb: is the fatted lamb, before it goes to the abattoir, food or not, given that once the lamb is slaughtered not everything is going to be consumed? That is the sort of issue that you are referring to, is it?

Mr Shepherd—That is right, exactly.

Senator O'CHEE—You can take the skin off it and you have got a hide, you can melt down the bones for tallow and you also have meat. Is that the sort of complex issue that would involve primary producers if you tried to exempt food?

Mr Shepherd—That is right, exactly. Not to try to be too flippant, but at what point does it move from being a family pet to being food? That is right.

Senator O'CHEE—I think some of my colleagues misunderstood the point you were making about compliance costs. The real issue with compliance costs is what you exempt, isn't it? Am I correct in understanding that if you exempt whole industries, the compliance cost impact is a lot less than exempting individual items or categories of items? Is that the case?

Mr Shepherd—We would argue from an economic perspective the lower number of exemptions you have, the lower will be the overall compliance cost to the economy. It is as simple as that. If you have 5,000 exemptions, different businesses and different industries around each one of those particular commodities that you have classified as an exemption will spend a lot of resources and effort getting advice as to whether they are in or outside the net and how they achieve this objective. That is the issue that we are trying to avoid.

Senator O'CHEE—Compliance costs include not just the cost of accounting it within your own business, but also the cost of getting advice as to whether something—

Mr Shepherd—That is the greatest compliance cost for small business.

Senator O'CHEE—For example, if you tried to exempt food and you had some definition of food, then you are saying that one of the consequences of that is that a whole lot of small businesses would have to rush off to accountants or lawyers to get advice as to whether what they sell constitutes food or not?

Mr Shepherd—Exactly, that is the issue. That is why we have been strongly supportive of the view that food should not be outside the GST tax base.

Senator O'CHEE—Thank you.

Senator SHERRY—I note you make the claim that lower personal income taxes will encourage greater national savings which will assist higher levels of business investment without causing a deterioration in the current account deficit. Further through your document you say that savings are increased if substituted for income taxes. Can you point me to any document showing real world examples where that has happened in the OECD?

Mr Shepherd—I cannot give you a clear-cut example of where there has been a shift in the tax base on those lines and it has resulted in an increase in savings. Again, I guess it is just a philosophical perspective that if you have a situation whereby you change the tax mix in such a way that you reduce the level of taxes on personal income tax, it does provide greater incentives than exist today. I guess it is more of a philosophical issue. In terms of trying to ascertain a country that has actually gone down this path and has resulted in increased levels of savings and investment, part of the problem of finding that sort of example, of course, is that it gets so caught up in other economic issues at the time. Trying to quarantine that effect from everything else that is going on in an economy is obviously very difficult.

Senator SHERRY—Why claim it? It is a fact, isn't it, that in the OECD countries that have introduced VATs or GSTs, whatever we choose to call them, and lowered income tax rates, there has not been an increase in saving?

Senator CONROY—Not in one country.

Senator SHERRY—That is a fact.

Mr Shepherd—I cannot give you the definitive answer to that. What we would argue on the whole is that countries which tend to have a lower incidence on income tax will generally have greater than average savings performance.

Senator SHERRY—It has not happened.

Mr Shepherd—If you did an analysis of a whole range of different industrialised or OECD economies—

Senator CONROY—So the US has got one of the worst then, given it does not have a GST?

Mr Shepherd—We are talking about two different things. What Senator Sherry is talking about is a situation where we are shifting the existing tax mix, asking what are the effects on economy through savings and investment, which is different from what I am talking about. What I am talking about is those economies which have already, for an historically long period of time, had a lower incidence of direct taxes: do those countries have different savings ratios? The answer to that tends to be yes. So there are two separate issues.

CHAIR—You are looking at the wrong indicator, are you not? Countries with a lower social security and welfare provision tend to have a higher savings ratio. That is, if the state does not provide you with a pension and you are taxed at a lower level because you are not provided for through the state, you invest in your own retirement security and build a higher level of private savings. That is the relationship, isn't it?

Mr Wojtkiw—It depends on whether you are talking about household or national savings and whether it is private or public. You are quite right, there is a mix there and it does vary depending on where the source of the income and savings is.

Mr Shepherd—Also, I would argue that clearly there is a range of economic variables which will impact on savings. Senator Cook has referred to the social security net and its impact on savings. It could well work on that basis. We have talked about the structure of the income tax system. There is a whole level of domestic interest rates; a whole range of factors work on the level of domestic savings.

Senator CONROY—Just in terms of those indirect tax figures—this was mentioned briefly in your presentation—the OECD revenue statistics show that the OECD average is 32 per cent reliant on indirect tax and Australia is 30 per cent. There is not some massive discrepancy. Those are the facts from the OECD.

Mr Shepherd—I guess there are a whole range of different measures.

Senator CONROY—I am using 1995 OECD revenue statistics on indirect taxation.

Mr Shepherd—We use *World Competitiveness Yearbook* 1996 figures published by the International Institute for Management Development, which show a picture pretty much the exact opposite of the one you have just painted. It is in our earlier paper of 1996 that, in terms of indirect tax revenues as a share of GDP, Australia was ranked 18 out of 46 industrialised and developing economies, at 8.9 per cent. So in terms of comparing Australia with the average experience of the countries included in the survey of indirect tax revenue as a share of GDP, Australia was approximately 0.9 per cent lower than the average of countries under examination, whereas in terms of personal income taxes Australia was approximately five percentage points higher than the average for countries involved in the survey. That is documented in the work that we did in 1996. So it depends what statistics you use.

CHAIR—Thank you, Mr Shepherd, Mr Wojtkiw and Mr Hristodoulidis, for your evidence. That concludes this section of the hearing. We will now adjourn for afternoon tea.

Proceedings suspended from 3.07 p.m. to 3.31 p.m.

HUNT, Ms Sarah, Senior Policy Adviser—General, Municipal Association of Victoria

MATHESON, Councillor Brad Anthony, President, Municipal Association of Victoria

SPARGO, Mr Robert Stephen, Member, Tax Reform Working Party, Municipal Association of Victoria

SPENCE, Mr Robert Norman, Chief Executive Officer, Municipal Association of Victoria

CHAIR—I welcome to the witness table the Municipal Association of Victoria. Mr Rob Spence is on my call list as the chief executive officer. Perhaps, Mr Spence, you would like to introduce those who are accompanying you. If you or whoever you nominate would then want to give an overview of your submission to this committee in brief form, supplemented by whomsoever you might choose at your table, you might then be kind enough to accept what I am sure will be a considerable number of questions from the committee.

Mr Spence—On my right are the President of the Municipal Association, Councillor Brad Matheson, who will make the presentation, and Mr Rob Spargo, who is the President of the Victorian Association of Municipal Accountants. On my left is Sarah Hunt, who is an employee of the Municipal Association. I will hand over to President Matheson.

Councillor Matheson—Thank you very much, Senators, for the opportunity to appear before you today to go through the issues surrounding what we consider to be a significant impact on our sector nationwide. The Municipal Association of Victoria, which is the peak body for Victoria—78 councils—views this with the utmost seriousness. There are, we believe, two major issues confronting local government in Victoria and nationally with respect to the proposed tax reforms as currently outlined in the draft legislation. They are the inclusion of local government in the GST loop, and the funding to local government and changes to the Commonwealth local government relationship. There are other issues on which we hope to go away today with clarification of what is actually intended, but we would also like to enlighten the committee about our concerns in that regard.

Under the current model, local government will pay a GST on all its purchases of goods and services, and the tax on these inputs will be reimbursed by the ATO. Also, local government will collect GST on its commercial activities. The outcomes which will affect local government relate to the fact that we will always be in a position of seeking reimbursement from the tax office for the GST collected. It would put local government on the back foot with respect to maintenance of services at current levels, which we have difficulty in affording to fund at the present time.

Local government will be placed in a position whereby it is forcing the community to pay GST on services where only a nominal fee or charge applies. These services are not commercial and are provided by councils in most cases because the private sector are not willing to do so. So it will have a dramatic effect in that regard.

We believe the cost of a GST administration is too high to justify collection. We believe from our analysis that about $400,000 per annum will be raised for a typical metropolitan council but about $3.5 million per annum will be reimbursed to the Australian Taxation Office, establishment costs could be as high as $1 million and, as I alluded to earlier, there will be reduced bank accounts of council funds of between $200,000 and $1 million, depending on the size of the council, and ongoing administrative costs of around $100,000. So it is going to cause a significant impost for administration. We have estimated that administration for every dollar collected would cost local councils around 25 cents.

Another point is the recovery of about $70 million. We do not believe that that is acceptable. I might hand over to Rob Spargo to perhaps run through that.

CHAIR—As you do, can I say you made the observation in your opening remarks, Councillor Matheson, that the committee may be able to enlighten you as to what is intended. I have to say I very much doubt it because I am not sure that the committee has a common view at all about anything at the moment.

Councillor Matheson—We have been seeking certain assurances from the Treasurer and they have not been forthcoming. I was hoping that perhaps some of the government members might be able to shed some light today.

CHAIR—The rest of us will listen avidly if they can.

Senator FERGUSON—Did you say they have or have not been forthcoming?

Councillor Matheson—They haven't been, no.

Mr Spargo—The tax reform package quoted a figure of $70 million a year being a saving available to local governments through the wash-out of existing taxes. To put that in perspective, local government spends, around Australia, $10 billion a year. Seventy thousand dollars is the estimated saving through wash-out of existing taxes and replacing it with the GST.

The costs to council have already been spoken of. So what we are looking at is the $70 million saving coming through a clawback arrangement, reviewing existing contract prices and future contract prices, and councils at all levels, large metropolitan and regional councils, being able to negotiate with their suppliers to be able to get those savings crystallised. An important factor in this is that the Municipal Association of Victoria has attempted, as has the ALGA, to source the data and the parameters for the estimate of $70 million and has been unable to do so. In short, the submitters cannot confirm the $70 million savings and in fact reject the notion of $70 million savings.

Councillor Matheson—If I can add to that, one of the issues that confront local government is that in many respects we are flying in the face of ignorance in terms of the impacts. There is scant information available to local governments in terms of what will and will not be exempted. The issues of exemption, whilst being put forward by the Treasurer in that the rate and certain charges will be exempted, are not illustrated in the legislation. Certainly, we would very much like to see that guaranteed by actually having those exemptions placed in the legislation. So that is certainly a major issue that we would like to take up with the committee as well.

With respect to the impacts on local government, we believe, given the impost on administration of the GST, that there really is no real economic or community benefit from the inclusion of local government in the GST loop. As I said, we are flying in the dark with respect to what will be GSTable. It appears that the majority of services provided which attract a fee or charge will attract the GST. I can give you a raft of services which will, I believe, detrimentally affect the community as a result—everything from the provision of sporting facilities for sporting clubs, local cricket clubs and football clubs, right through to the hire of baby capsules, through to the provision of a range of services which councils provide to the community—and, may I say, in many areas of the community which would otherwise be vulnerable in terms of their needs and certainly in the reliance that they place on council support.

ACTING CHAIR (Senator Ferguson)—Mr Spence or Ms Hunt, do you wish to make any comment at this stage?

Mr Spence—The issue that I wanted to comment on was in relation to the grants process. There is a major issue for local government in relation to the transfer of responsibility for distribution of grants and granting levels from the Commonwealth to the state. As an association we have concerns about that resting with the states. We are particularly concerned about the level of grant that is proposed in the legislation. There is an assumption in the legislation that the level of grant going to local government is the appropriate level at this particular point in time and that the proposal is that it will be fixed on a per capita real term basis.

Certainly, when you look at the Grants Commission data from the Victorian Grants Commission, councils are getting under 50 per cent of need from the process. We would argue that the level of distribution of tax through the states to local government in Victoria should be significantly higher than the level it is at the moment.

The second point about the process for the distribution is that it is the view of local government across Australia that that distribution should still occur under a Commonwealth mechanism. Certainly you would understand in Victoria's case that local government would be very nervous about the relationship with the state government and grants given the level of reform and the relationship issues that we have in Victoria at this particular point in time. We believe that it is important that we shore up a long-term relationship between local government and the federal government.

Councillor Matheson—Adding to Mr Spence's comments, we do not want to see the relationship between the Commonwealth and local government severed. Effectively, these sets of reforms actually sever that relationship. We believe that the relationship has worked well to date. Certainly it has provided in many respects a circuit-breaker between local and state governments. We would like to see that relationship maintained with respect to the grants formula and process.

Senator GIBSON—With regard to those grants, is it not true that, under ANTS, the government is proposing that the states are going to be the recipients of the GST revenue and that part of that will be the 1.6 per cent that goes to local government, but that one of the conditions of passing over that revenue is that the states sign off on continuing the funding to local government as of today? Isn’t that so?

Mr Spence—That is correct. It is our contention that that level is too low. What the GST is proposing is potentially real growth in state revenue through the GST, but what it is doing is locking local government into a significant cash deficit. That either means that you have to put up rates to recover dollars over time, or you have to decrease services. As I say, the Grants Commission process that is run in Victoria is showing that councils are getting back through the grants process about 45 to 50 per cent of need.

A study has just been completed in Victoria, and it is still in draft form, by the Office of Local Government. It is showing that there is an infrastructure gap in Victoria, simply for maintenance of the assets out there in councils, of about $230 million. That is not including the issue of replacement and establishment of new assets.

Senator MURRAY—Is that per annum or once off?

Mr Spence—That is per annum. It is multiplying over time. I think if you look across Australia you will find that this gap is there. When the Grants Commission model was put in place it was the grants model. I think it was in the 1970s. As I understand it, the objective was to overcome some of these imbalances in need. There is a significant imbalance.

I take your point in relation to what is proposed. We are arguing that what is proposed is not good enough and that there should be a level of growth in the amount of money that is distributed to local government through the process and that we have an in principle objection to the states distributing it. It is a question of what relationship we have with the Commonwealth. Is local government going to be totally a child of the states? It is our contention that it should not be.

Mr Matheson—If I may add in support of that, you only have to look at the national competition payments to Victoria for the reforms that were undertaken in local government. Local government shared in nine per cent of the actual total. That really does set the cat among the pigeons with respect to the funding relationship that could very well transpire as an outcome of these taxation reforms between state and local government.

Senator GIBSON—Is it true that you are set up under state legislation in each state?

Mr Matheson—That is correct. You are a child of the states.

Senator GIBSON—While I hear what you are saying about the future, with the change in the taxation arrangements, assuming ANTS goes through as the government has outlined, you will be no worse off immediately after the introduction than you are today.

Mr Spence—That is true, but what I am saying is that there is an assumption that what we are getting at the moment is right and I am saying that that is incorrect. It is a very easy solution to say we will just continue to give you what you have, without doing any assessment of whether that is the appropriate sum of money; whereas, you are offering the states growth revenue.

ACTING CHAIR—You are arguing two different cases here. You are saying that the level of funding is not high enough under the current arrangement, but then you are saying that you do not want the states to fund, that you want the federal government to be responsible. You are actually arguing two different cases.

Mr Spence—We are. We are arguing one case which says, as a point of principle—and this is across all local government associations in Australia—that the distribution should be via the Commonwealth and under Commonwealth control, as it is at the moment. The second point we are making is that in any event the level of distribution is inappropriate—it is too low.

Mr Matheson—The basic assumptions are flawed.

Mr Spence—Yes.

Senator MURRAY—The last point you made is the point that impressed me with the local government approach. I would have assumed that local government attitudes would vary according to their experience with their particular state government. Yet regardless of the state governments, my understanding is that all local government associations, from every state and territory, support this approach. Is that correct?

Mr Spence—That is correct.

Senator MURRAY—I have assumed that that is because you know the set-up with the Commonwealth and how that works; whereas if you revert to the states, I assume that in every state constitution you have no guarantee with that either, have you? The relationship between local government and the state government is not spelled out in the Victorian constitution.

Mr Matheson—No.

Senator MURRAY—Nor is it in the Western Australian constitution. Is there any state or territory where it is spelt out?

Mr Matheson—I believe it is spelt out in the Queensland constitution.

Senator MURRAY—And do they feel more secure because it is in that Queensland constitution?

Mr Spence—The relationship between the Queensland association and local government and the state is probably the best in Australia, the strongest.

Mr Matheson—And that is reflected across governments. It has not just been a Labor government. It has been a former Liberal-National Party government where they have enjoyed a very close relationship with the local government sector.

Senator MURRAY—Would you agree that it is difficult for the federal government to even contemplate changing the federal constitution, that it is almost impossible for them to guarantee local government will be catered for in state constitutions?

Mr Matheson—That is right.

Senator MURRAY—So your approach is built on the basis of the precautionary principle that you have understood the basis on which the Commonwealth has dealt with you in the past and you fear the basis on which states will deal with you.

Mr Matheson—Yes.

Mr Spence—That is correct. Local government is a significant player in Australia and it is our view that, if we lose this link, then there is no real link with the Commonwealth government.

Mr Matheson—Some of the detractors of local government will say, 'We are a child of the state.' If you took it to its nth degree with the Victorian government, they would say, 'We are no more than service delivery agencies of the state out there in the suburbs.' Local government sees itself as much more important than that.

Senator MURRAY—Is your association dominated by any particular political flavour?

Councillor Matheson—We are an ecumenical church. We have a very broad range of people who represent issues first rather than political parties. The issues are such in Victoria that you cannot afford to have factionalism or party politics involved in local government at peak level. Certainly, with people coming from a range of backgrounds, the MAV and the councils are really addressing the issues.

Senator MURRAY—Are there any councils in Victoria which disagree with the association's stance?

Mr Spence—The association's stance has been developed by a committee of councils and council officers and has been tested with our constituency, and we have had no negative feedback.

Councillor Matheson—It meets with their approval.

Mr Spence—It is from all sides of the political spectrum.

Councillor Matheson—The government's constituency out there in regional Victoria is very concerned, given the impact on the smaller shires and remote municipalities where it will have a dramatic effect.

Senator MURRAY—I think Senator Ferguson's comment, if I understood it correctly, was a good one. How have you tested their support for your stance? Do people sign up on it? Have they been surveyed? How do you do it?

Mr Spence—We have run the process through a committee that has had both rural and metropolitan councils on it. The councils have had the option of nominating their people. No-one has been excluded. We have run a full process there that has had, as I say, the full scope of representation, and we have kept our membership informed.

We have had positive feedback from a number of councils that are on the right. You would expect to see some councils on the left of centre that would support our position, but we have certainly had positive feedback from councils on the right. And nobody has argued about the position we have taken.

Councillor Matheson—As president, I speak to the 78 mayors and council representatives on a regular basis, and they are as one on the effects of a GST on local government. Each of them endorsed our actions last year, prior to the federal election, to survey local federal members of parliament with respect to the impact in their local communities. I cannot speak for every one of the councillors out there but I can assure you that the 78 councils support what we are currently undertaking.

Mr Spence—To my mind it is a pretty difficult argument to argue against from a council's viewpoint. We are talking about costs going up 25c for every dollar they collect. Councils have no obvious capacity to recover that increase other than by cutting services or putting up the rate, or finding some other solution to their revenue streams. Councils have complained, probably for the last 10 or 15 years in Victoria, about funding for roads from the Commonwealth, or about infrastructure from the Commonwealth, or about the general grants distribution from the Commonwealth. This proposal is not giving councils anything, just cost.

Senator MURRAY—The argument we have heard from business organisations is that from a compliance point of view it is better for them either to be completely GST free or to be completely GST inclusive. Regardless of your success or otherwise, there are going to be some areas in which you have to comply with GST matters and other areas where you may not. Would you rather incur the compliance costs by having some of your activities GST free in preference to having everything with GST on?

Mr Spence—The dilemma with the compliance costs is that the systems costs are going to be there whether it is all in or part in. Councils in Victoria have not got accounting systems that can deal with a tax because we have never had to collect a tax. It means that every accounting system in every council, on our estimate, will have to be upgraded to deal with it. So there are massive up-front costs.

Senator MURRAY—So if the government wanted to reject your position because they might argue that your compliance costs would go up if they increased the range of items which were GST free, you would argue that that is irrelevant. Is that what you are saying?

Mr Spence—If our argument is rejected, then we need a model that absolutely minimises the dollar cost on councils. There are some possibilities as to how you do that. The Vos report suggested some in terms of supporting organisations that have big input costs and big input tax, and low revenue coming in from the GST. So there are ways to structure it where you minimise the cost. Our view is that because only about six per cent of councils' business gets picked up by a GST anyway, why have us in the loop? There are massive compliance costs and administrative costs to deliver a relatively small outcome. But if the government decides they want to go down that path, then we need to be getting almost immediate reimbursement for the amounts that we are paying by way of the GST, we need to get cash support up front to allow the systems changes to occur and we have to find ways to minimise the ongoing costs to councils.

Senator MURRAY—Thank you.

Senator O'CHEE—I am sorry but I really do not understand the rationale, so I thought it might be better to take you through it.

Senator HARRADINE—Excuse me, Senator. Mr Chairman, I apologise, but I have to go. I have to go up to Canberra for another committee meeting.

Senator O'CHEE—Mr Spence, at page 4 of your submission you say that for every dollar you collect it is going to cost you 25c. Yet, at page 8, you say that only six per cent of your total revenue will be subject to GST. You just spoke about a massive administration task. Surely, your administration task breaks down into two parts: one is collection of the GST and the other is claiming your rebate back. Surely, for the collection of the GST, given that you can clearly identify the fees and charges which are subject to the GST, you just take one-eleventh of that.

Mr Spence—I will hand over to Rob who can take you through the detail of it.

Mr Spargo—There are in fact four parts to the cost to councils of GST administration. Councils will generally pay out 10 times as much GST as they collect—as a rule of thumb. Of the councils' total revenue, only six per cent will be subject to GST; of their expenses, about 60 per cent will be subject to GST. So councils will be paying out about 10 times the amount of GST they collect. Because of that, in any given month, councils will have a cash flow problem—they will have cash out waiting to come back.

Our models show that if councils submit monthly claims by the seventh of each month, a normal council could expect to have somewhere between a $200,000 and $300,000 permanent reduction in their bank account. If a council chose to do the quarterly returns, as would be the case because of the size being under $20 million in revenue, then a medium size council in Victoria would have a permanent reduction of about $1 million in cash flow because they are paying out and waiting for the cash to come back. So part of the cost is the financing of that cash flow and the lost interest on that cash flow.

Senator O'CHEE—Five per cent on $200,000 is $10,000 a year?

Mr Spargo—Yes. It will reach peaks at various stages through the year. Some councils will have five per cent, some will have overdraft charges much higher than that. In addition, for each invoice that is processed through the council—this is when we are paying accounts—we will need additional coding and additional key-punching to be able to identify the GST.

Senator O'CHEE—The conceptual difficulty that I have with what you are saying is that you do not account for the GST item by item. You account for the GST at the end of the period. I am not asking you to itemise the GST on two spare tyres, four cans of paint or 50 rubbish bins. We are saying, 'These are your purchases. The entirety of the purchases you divide by 11 to work out the—'

Mr Spargo—I am aware of that situation. I am also aware of the audit situation that is required that people only claim back the value of GST on taxed invoices that they have to support each claim. In the tax audit, one can expect a number to be there of the claim that has been put in and the councils will have to substantiate that by identifying invoices on which GST is paid.

Senator O'CHEE—But when the council prepares its accounts or it does its budget at the end of the year, it does not break down the accounts into every order for rubbish bins, every order for paint or whatever. It puts them into general categories.

Mr Spargo—Yes.

Senator O'CHEE—That is subject to the same audit rules to which you have just referred. Why is it different?

Mr Spargo—Because the legislation that is proposed requires council to have a taxed invoice for each claim. If we want to claim $100, we have to show a taxed invoice for $100.

Senator O'CHEE—We ask you to have an invoice for every claimed expense now but you do not, when you prepare your accounts, itemise every individual item. You just put it into a category. There is no difference between the substantiation required for income tax purposes and the substantiation required for GST purposes. I think Mr Spence, by his nodding, acknowledges that point.

Mr Spence—I am absorbing what you are saying. I find it a bit hard to understand how you can avoid the audit trail between the grossed-up numbers and the individual numbers. When the ATO rock into a council and they want to go through the numbers, are you telling me that we do not have to have a trail back from the aggregated numbers to the individual numbers?

Senator O'CHEE—It is the same as the trail you prepare for your accounts at the end of the year. You have got aggregated numbers and you have individual numbers.

Mr Spence—But we are talking about 60 per cent, say, on $80 million. The services that are provided across a council are enormous in range—hundreds literally. Of those, some of them are out of the loop and some of them are in. You have actually got to be able to break up what is in and what is out, as well.

Senator O'CHEE—No other business that has come before us genuinely believes it has to break the GST down invoice by invoice. Nobody else has actually said that that is a problem. Every other business that has come before us accepts the fact that you account in toto. You might have different categories in which things fall but nobody hitherto has said that they believe they have to account invoice by invoice. They accept that the returns are based in toto.

Mr Spence—The argument I am putting to you is that if the total of your business is subject to the tax, then it is possible to actually gross it up by 10 per cent.

Senator O'CHEE—But, surely, you know what categories are what?

Mr Spence—I do not think it is that clear in terms of individual expenditure lines. But the trail still has to be there.

Senator O'CHEE—It is a very simple—

CHAIR—Order! We are getting into debating the evidence, I think.

Senator O'CHEE—I am just trying to ascertain exactly why they believe it is, Mr Chairman.

CHAIR—Indeed. The question was originally Senator Murray's and you took up the point—

Senator O'CHEE—Senator Murray had concluded, I think.

CHAIR—I am not sure that he has.

Senator O'CHEE—If he has not, I am happy to cede to him.

CHAIR—All I was wanting to do was to give you a reasonable chance to pursue that point which, I think, I have. But if there is a question or two that you need to conclude your foray, please take those questions. But I want to move the call around if I may.

Senator O'CHEE—Sure.

CHAIR—And if it is Senator Murray that wants it, I want to give it back to him.

Senator O'CHEE—Can I just go to the other point that you raised? I am waiting to see where you get to 25 cents for every dollar of revenue. The other point is that nowhere in this document have I seen any calculation of the saving to councils through the reduction in fuel costs. The Queensland Local Government Association says that it is a very substantial cost saving. They say that even the Brisbane City Council will save $13 million a year just on diesel. That is not accounted for in this document.

Mr Spargo—To take the first part of your question on where the 25c comes from: the choice in action of the councils will be, I am sure, to be able to provide an audit trail from the invoice to the tax collection and with the tyres, for example, to be able to make sure that the stock held in stock is its tax-free price. You need to take the tax out of stock holdings so that is the value of them. We believe that every invoice would need to be done that way. We would estimate that that would be a 15 per cent increase in key punching and $30,000.

We have also allowed ourselves $5,000 for audit in each year for audit fees associated with this and for the general staff training, accounting and reporting. We have allowed $45,000 for having it go through and making sure that we conform with the administrative arrangements; $95,000 for a council which would, on average, collect $400,000 in revenue and pass forward; $400,000 on revenue is 25c for every dollar passed forward. That 25c is a cost borne by the community.

Senator O'CHEE—Can I just say that I think that is a bit of an ambit claim? I do not want to get into a debate about it because we could deal with this all day. Let us get into the issue of the fuel. Where have you put that in the savings?

Mr Spargo—We have not included savings on the diesel fuel excise. We have not been able to substantiate the $70 million which was previously in the tax reform paper as a saving.

Senator O'CHEE—You must know how much diesel fuel councils consume in Victoria a year.

Mr Spargo—I do not know how much diesel fuel councils consume.

Mr Spence—I do not know.

Senator O'CHEE—Could you take that on notice and maybe we could work back through that.

Mr Spence—We are happy to provide additional information at your request. We tried to make the point about the $70 million at the start of the presentation. We have had difficulty getting from the Commonwealth government how they calculated the $70 million. There is a component of that that is a significant one and that is how we claw back the embedded sales taxes. There is a view that has been expressed to us that a component of that $70 million across councils is embedded sales tax and we should be able to claw that back. There is an argument as to whether we are capable of doing that. But we are happy to provide any information that you want.

Senator SHERRY—I would like to run through and get an indication of the sorts of services in which charges will apply. Before I do, is it correct to summarise your basic problem as being one of charging for a vast array of services and the charges are quite small for a large number of transactions?

Mr Matheson—That is correct across all council services.

Senator SHERRY—Let us just go through some of those services. You have mentioned sporting fields, cricket, football et cetera—and I think I heard baby capsules?

Mr Matheson—Yes, baby capsules will be subject to a GST.

Mr Spence—The hire of baby capsules. In Victoria, councils hire baby capsules to people when the baby is born and they have them for a period of time. They hire them from the council instead of having to buy them. In the needy communities that ensures that people actually have state-of-the-art baby capsules in their cars. It used to be funded by the state but they cut the funding out. A significant number of councils across Victoria still carry that service. I could get you the number.

Senator SHERRY—Fine.

Senator FERGUSON—Do you know this cost individually?

Mr Spence—I have just bought a couple of them. It is nearly $250.

Senator FERGUSON—No, the cost of actually hiring them.

Mr Spence—The costs are minor.

Ms Hunt—It is about $70 per annum for a hire.

Senator SHERRY—Swimming pools?

Mr Matheson—Fees for swimming pools, yes.

Senator SHERRY—Community halls?

Mr Matheson—Yes, the hire of community halls, any community recreational facility.

Senator SHERRY—What about transport facilities?

Councillor Matheson—Community buses would be subject to a GST. They are widely used, particularly with our seniors.

Senator SHERRY—That was my next question. I had assumed that seniors' services were fairly common. Any other forms of transport?

Mr Spargo—Not that I am aware of.

Senator SHERRY—Equipment hire. We mentioned baby capsules. Do councils rent any other form of equipment?

Mr Spence—Some councils provide equipment, sporting equipment and so on to people. There is a wide range. We are trying to actually track down the level of services that is provided at the moment. It is massive.

Senator SHERRY—Libraries—what is the situation with libraries run by local government?

Mr Spargo—Libraries are part funded from government, and there are no charges on library services. There are for books and publications, and there are some charges for photocopying and fines.

Senator CONROY—That is the late fee?

Mr Spargo—Late fees, those types of things.

Councillor Matheson—There is now a fee on Internet services which most councils are picking up on.

Ms Hunt—The other thing with the library is things like the training provided through the libraries, Internet training to use facilities within the libraries.

Senator SHERRY—Parking?

Councillor Matheson—Certainly parking fines. Sitting in the great city of Melbourne it is going to cost them—

Mr Spence—Parking meters?

Councillor Matheson—Parking meters. It is going to cost them $1.3 million to reconfigure their parking machines in this city.

Mr Spence—Every parking meter needs to be ramped up by 10c or you need to find a way of dealing with it.

Senator SHERRY—How will you do that, just as a matter of practical—

Councillor Matheson—You would have to chop the heads off and put new heads on.

Mr Spence—You either absorb it internally—and that is one option which I do not think you will see many councils willing to do, given the state of their finances—or you could actually adjust each machine and reduce the amount of time.

Senator SHERRY—There is obviously a cost in that.

Mr Spargo—I would like to say the machines take either $1 or $2 coins, and it makes it difficult to add 10 per cent if they only take those two varieties of coins.

Senator SHERRY—Nurseries? Do any councils run nurseries?

Councillor Matheson—Yes, most councils run nurseries. Nurseries as in?

Senator SHERRY—As in plant nurseries?

Councillor Matheson—Plant nurseries, yes.

Senator SHERRY—And the human as well, I suppose?

Councillor Matheson—Yes, and the human.

Mr Spence—There are plant nurseries around. There are lots of human nurseries around. Plant nurseries, yes, and there are some sales from plant nurseries. They are used to service your own stock requirements, rather than buying the stuff.

Senator SHERRY—Whilst on nurseries, dog and cat kennels?

Mr Spence—Not so common in Victoria. Certainly we have pounds.

Senator CONROY—But the pounds. The pound collection, if you are going to collect it, when you pick up the pooch.

Senator SHERRY—Publications?

Mr Spence—We have a wide range of publications, most of them community benefit-type things. We give some away, but there is a significant number you would sell as the costs are too high.

Senator SHERRY—And that would include maps?

Mr Spence—Maps.

Senator SHERRY—What about maps for someone who wants to buy a house, for example, or if they want a survey map, a property map?

Mr Spargo—There is a certificate issued by councils to people who are buying houses. In Victoria they are called land information certificates, and they have all the property details and flood levels on those, and they have a statutory charge to them.

Senator SHERRY—I was going to get to that issue in a moment. But if you went into a council and wanted a photocopy of a map for a reason, and there was a charge made?

Councillor Matheson—You would certainly pay for it.

Senator SHERRY—You would pay for that; okay. One other area that I was not sure about is building inspections and plan approvals. Are they statutory charges and, therefore, exempt?

Mr Spence—Moot point, I think.

Councillor Matheson—Still unclear.

Senator SHERRY—You do not know. Are there any other categories of charge that we have not discussed that you can think of?

Councillor Matheson—A lot of councils do engage in recycling and there are waste charges which are actually added to the yearly bill. They are not part of the rates.

Senator CONROY—They are separate from the rates?

Councillor Matheson—They are separate from the rates. There are waste charges. That is to promote recycling and, if that is affected, then that is going to have a detrimental effect on the already problematic contract relationship between recyclers and councils.

Senator SHERRY—I am aware in Tasmania where I come from that there has been concern amongst councils anyway at the difficulties of maintaining their recycling services, aside from this particular issue. So we have a multitude of—

CHAIR—Could I just ask one of my favourites? I come from Western Australia, and my local council has offered a service to clean graffiti off walls of ratepayers. I am not sure if I have to pay for it. Is there a similar arrangement with any councils in Victoria? If so, is there a charge?

Councillor Matheson—There are councils that provide those services. They are not provided across the board, but certainly there are a range of services which are run by councils individually. I have certainly heard of that being run here in some councils.

Mr Spence—And there would be a fee for it. It depends who it is targeted to, but generally it is towards the needy end of your residents. It is like gardening services for the elderly that are provided by the council, and they would attract a GST.

CHAIR—Someone sprays on my wall before every election, ‘Whoever you vote for, a politician always gets in.’

Senator SHERRY—I just want to clarify this point: you said that some councils provide gardening services to the elderly.

Councillor Matheson—Yes.

Mr Spence—The range of services where there are fees applied by councils is quite large. Councils mix and match relative to their own need and their municipality.

Senator CONROY—Is heavy rubbish collection a separate fee or is that included—

Mr Spence—Some councils pick it up as part of their garbage rate, others have a separate fee for it. Some are also contracted out to a private contractor.

Senator CONROY—A subcontracting out situation would see a fee applied—

Mr Spence—It would be a fee applied by the contractor.

Senator CONROY—Is any actual garbage collection done in that way that would be separate from the rates because it is subcontracted?

Mr Spence—The normal garbage service comes under a garbage charge. Some councils include the garbage charge as part of the rate. Some have a separate garbage charge, and that is used to finance the garbage service.

Councillor Matheson—We run three in our city: one of garden waste, one of putrescible waste and one for recyclables—two of which are not covered within the rate.

Senator CONROY—If the garbage rate is outside the rate, would that garbage collection rate come under the GST?

Mr Spence—No-one is saying that it is not at this stage.

Senator FERGUSON—Is there any reason why you should not put them in the rates? The rates are GST free.

Councillor Matheson—That is speculative too.

Senator FERGUSON—No, it is not.

Councillor Matheson—Yes, it is.

Senator SHERRY—If it is put in the general rate, isn't it a problem for people who do not have a garbage service?

Mr Spargo—The collection of household garbage is required by councils under the Health Act. Whether you have a bin or not, part of your cost in your rate is for that service. There are very few that do not have bins. The reason that some councils choose to take a garbage collection as a separate charge is because they can influence people's decision on what size bin they have. If it is wrapped back in and made GST free that is one method of influencing behaviour that will be denied to local government.

Senator SHERRY—So there is a good environmental reason for attempting to influence the collection or separation habits of consumers because it is cheaper to do it at the point of collection rather than later on trying to separate it.

Councillor Matheson—Kerb side collection is the point, and recycling has been one of the more successful campaigns that we have run locally.

Senator SHERRY—From what I am gathering, a considerable range of your services will be subject to a GST. In terms of individual revenue collection they are quite small, and in terms of a proportion of a council's total income they are quite small; hence the significant administrative cost because of the sheer number and volume of them.

Mr Spence—That is right.

Senator CONROY—There seems to be some confusion between Senator Ferguson and ourselves. Are you able to point to the page where rates are exempt within the legislation?

Councillor Matheson—There is nothing in the legislation that exempts rates. There is nothing that you can point to. It is really only exempted at the minister's discretion. There is nothing that could stop the minister from changing his mind once the legislation is adopted. And that goes for all of the exemptions. There are no exemptions in the legislation. What we would like to see is exemptions guaranteed in black and white in the legislation.

Senator GIBSON—To follow up Senator Sherry's question about those services that you provide: do you believe that councils ought to have a commercial advantage—by being GST free—over private sector suppliers?

Mr Spence—No, we do not. In our submission we are saying that in the majority of these services, in a very high proportion of them, we are the only provider. We are providing a service that is really subsidised anyway. Rarely would any of these services be in at full cost. A significant proportion of these services are not targeted at the whole of the community; they are targeted at the needy end of the community.

Senator FERGUSON—In actual fact, in your submission you say that you want local government to be left out of the GST 'loop', to use your word. If you are going to be left out of the GST loop, what you are asking us is that your commercial operations be GST free, as opposed to commercial activities run by private enterprise—who will not be GST free—and your councils. If you want to be outside of the loop, that is what you are asking us to do.

Councillor Matheson—The vast majority of services that we provide are not provided by the public sector. We provide them because they are not being provided and are not marketable to the public sector.

Senator FERGUSON—But you are not talking about a vast majority. You say you want to be outside the loop. In my own instance, where the local government runs the local caravan park and there is a private operator alongside, if you want to be outside of the loop you would be asking us to let the council-run caravan park be GST free when the local private operator will have to pay a GST. Where is the fairness in that?

Mr Spence—I take your point. If you look the components of council activities that are actually in the commercial environment, however, you are talking about a very, very small proportion. We are talking about six per cent of our total revenue base being subject to a GST. I think you would find, if you did the analysis on the level of it that is commercial, that it is a very, very small component.

Senator FERGUSON—It varies from council to council. Some councils subcontract out their garbage collection; some do it themselves. There is a whole range of commercial activities within local government. If you say that you want to be outside of the loop, to use your term—I have never heard the GST called a loop before; a broad based tax generally means that it covers everything—then you are asking for special treatment that is not available to private operators.

Mr Spence—I think the term 'loop' is a pretty good description in the case of Victorian local government because we are actually involved in a dance to pay out money and get it back, with very little ultimate revenue going to the Commonwealth but at what we would argue is relatively significant cost to the councils. That is where the term ‘loop’ comes from. We are not talking in the jargon of the legislation. It is a loop for us. There is a lot of administrative cost for not significant benefit, and a large imposition on councils. That is where the term comes from.

There is an argument at the fringe about what is commercial and what is not. In local government in Victoria, you will find, the garbage services are funded by the council. In a significant number of cases there is a subsidy in it. The revenue stream is collected by way of a charge; there is some subsidy in it by way of rate and, where a private contractor is contracted to provide the service, the revenue stream actually comes in through the council. They are not raising their own revenue.

Senator FERGUSON—You still have not really answered my question. I will only ask it once more to see if I can get an answer. If your local government ran a caravan park alongside of a private operator in the same area who was running an equivalent caravan park, do you think it would be fair that the council operation should be GST free and the private operator not?

Mr Spence—I do not. Our association would not argue that. What we are saying is that when you look at the totality of the position, there is questionable benefit for us in being involved in the GST loop.

Senator FERGUSON—If you are not going to be in the loop, though, you are going to leave that situation, aren’t you?

Mr Spence—There is an argument that says there are no anomalies in this legislation. What I am saying to you is that when push comes to shove, at the tail end of the things that impact on local government this is a very small proportion of the total. We are not generally in a commercial environment.

CHAIR—Let me interpret it myself to see if you agree. Where you are in competition with the private sector you agree on the principle of competitive neutrality?

Mr Spence—Definitely.

CHAIR—Where you are not, you would wish to be excused from the ‘loop’?

Mr Spence—Yes.

Senator SHERRY—There are just a couple of points I wanted to raise on this issue. Presumably there would not be very many private operators providing community halls, cricket, football, et cetera—certainly not at cost, I would have thought.

Mr Spence—Some councils would argue that they wish there were some commercial operators out there, but there are not. Basically these are services provided by councils, who are the only ones in there.

Senator SHERRY—The same with libraries? I don't know of any private libraries.

Mr Spence—Libraries are the same. In the competitive tendering environment in Victoria, libraries have been put through the tendering loop yet I do not think we have any players in the library market now apart from councils—a couple of regional bodies that are made up of a number of councils.

Councillor Matheson—They are generally won by in-house bids.

Senator SHERRY—To return to the issue that Senator Ferguson raised about competitive neutrality: isn't it a little difficult to apply that, for example, to swimming pools? There are privately operated swimming pools. It is relatively common. But there would be some areas of regional Australia, in the outback, where it just would not be possible to have a privately built, constructed and operated swimming pool. There would not be the necessary level of demand. In a small town in Tasmania—Campbell Town, I think—the community built a swimming pool with council support and it is run by the council. So it is not an easy principle to apply, is it, particularly in areas where presumably it is hard to attract a private operator in competition.

Councillor Matheson—If I may just add to that: where you have had amalgamation of some shires out in remote Victoria, or the amalgamation of five or six municipalities, five or six swimming pools have been inherited. So there is actually a need to close down some swimming pools and rationalise some of that asset.

Senator SHERRY—One final point: presumably a lot of the community halls were memorial halls built after World War I and World War II, weren't they? Certainly in my home state of Tasmania a lot of them were built in memory of ex-servicemen.

Mr Spence—There is a whole range of halls out there, from former military halls that have been taken over by councils after the Second World War through to—

Councillor Matheson—Town halls—there are surplus town halls aplenty in Victoria at the moment.

Ms Hunt—Community centres as well are springing up now, which have a wide usage.

Mr Spence—On the leisure centre question: you do not generally see leisure centres, of the size and complexity that councils provide, provided by the private sector. I think that is a fair assumption. What you get from the private sector is generally small pools with large gym space, whereas when you have got major facilities such as large swimming pools with a whole range of features the capital is generally provided by councils, because it requires a significant local subsidy to make it happen. It is not a revenue generator.

Councillor Matheson—In my municipality we are looking to build a hydrotherapy pool for the ageing community. That is going to attract a GST.

Senator FERGUSON—You have concentrated on the effect. In this inquiry we are talking about a new tax system, not just about a GST, but all of your contribution has been in relation to the GST and its charges. At no stage have you mentioned that some charges may rise because of the GST, by a certain percentage. At no stage have you recognised the fact that the government has offered significant income tax cuts to your ratepayers, or significant compensation to those who are not wage and salary earners, in order to accommodate any small rises that might occur as a result of what you have said would only be small fee rises on an individual basis.

To follow on from Senator Sherry’s question, where I can see a very lengthy press release coming out: he is trying to explain to you the effect there will be on the community of all these extra little tiny fees and charges all accumulated, whereas the compensation through both income tax cuts and the compensation package was put in place to allow people to pay for any extra charges that might occur. The Treasurer’s estimate is that still, overall, the impact on the CPI, which would include local government charges, will be 1.9 per cent.

CHAIR—Is that a question or a statement?

Senator FERGUSON—I am trying to put into perspective all of the things that have been raised.

CHAIR—I am just asking whether you are asking a question.

Senator FERGUSON—I am trying to suggest to you, if it is the extra charges that you are worried about, that in fact the compensation package is put in place to make sure that people have the wherewithal to combat any small increases in charges.

Mr Spence—I think that is outside the scope of our capacity to analyse. At this point in time nobody that I am aware of has been able to analyse the implications of this package for a pensioner in Sunshine. All we are trying to do is bring to you a perspective from local government on what is going to happen, because there seems to be a range of views about the way local government will be impacted. We are trying to demonstrate to you what we think are the issues.

CHAIR—Thank you. I will excuse you but I have a question. In any work that you may have done in anticipation of a GST being introduced, you would be aware, no doubt, of the debate about pass through—that is to say, by the removal of some taxes, some goods will be cheaper. The argument is whether or not that saving is passed through to the consumer at 100 per cent of the saving, or whether it is retarded in time and then passed through, or whether it is passed through at less than 100 per cent of the saving.

To a very large extent, local government is a consumer of various of those products that might have a lower price if there were 100 per cent pass through. That is the background against which I ask my question. Have you looked at this issue, and do you anticipate that you will in fact receive a 100 per cent pass through or have you budgeted for less than that?

Mr Spargo—The impact on local government of removing some taxes and adding the GST has two facets to it. One is that local government is not subject to the wholesale sales tax, with the exclusion of some vehicles bought for private use. We would see that the computers that we buy, which currently do not have a wholesale sales tax added to their price, will attract a GST and will be at an additional cost. So there are some things which councils do not pay tax on but that will in the future have taxes paid on them.

Under the clawback arrangement, where we engage somebody to mow our lawns who has a diesel tractor and will receive a diesel fuel rebate or some of the other taxes that might be incurred, how to extract or draw or claw back that cost saving is a major problem for local government, who have literally thousands of individual contracts for services throughout. How they identify those and enforce those things at the local level is problematic.

CHAIR—You will always have the GST police, the ACCC, to help you. The ACCC is apparently the disciplinarian or policeman in this area.

Mr Spargo—Yes, and I believe that councils need to build partnerships with their providers. Sourcing back into their data and to their suppliers' data—whoever is the last one in the food chain that actually supplies the services—is very difficult. Councils can build up a partnership with one supplier, but if they are buying their paints and paintbrushes from another, how does that work all the way through? It was on this very point, the $70 million that the tax reform package said was the saving for local government, that the ALGA had asked for information, asking for the parameters on which that was based and the various components of that, but we were unable to be satisfied with the data. It is an area where there may be savings. As to how to extract those, I guess local government will not be any different from any other company that is trying to do that.

CHAIR—If I may, I would like to put you to a little trouble. You have indicated that there will be areas where you do not pay tax now—that is, the purchase of computers—but where you will under a GST. Is it possible for you to give this committee—I ask this question on notice to you—some sort of broadsheet setting out what items you might need to purchase in the running of a council that will now attract a tax, if there is a GST, which you do not pay tax on currently?

Councillor Matheson—Yes.

Mr Spargo—Every payment that the council makes, with the exclusion of salaries and wages, will attract a GST. Currently the only wholesale sales tax that council pays is on private use vehicles. This is 22 per cent which, for most councils, is paid on a very small number of vehicles each year. Councils will go from virtually a zero taxation to somewhere around 55 to 60 per cent of their expenditure being subject to GST.

CHAIR—That is, 55 to 60 per cent—I am quoting back to you what I think were your figures—of expenditures will now attract a GST?

Mr Spargo—Yes.

Mr Spence—Subject to rebates.

Senator FERGUSON—How much of that 55 to 60 per cent would be rebatable?.

Mr Spargo—Virtually all of it. Very minor areas—

CHAIR—But you will have to carry it until it is rebated?

Mr Spargo—That is right.

Senator FERGUSON—Like every other business.

Senator MURRAY—There is one question which arises from all that, and that is this: if the government legislation were changed to fix your cash flow problem—that is, to allow you greater time—would that meet a lot of your concerns?

Mr Spence—It would. The resolution of the up-front financial support issues to deal with the administration costs—computer system changes and whatever is required—and then the resolution of the cash flow issues would go a long way to resolving our concern.

Senator MURRAY—Dealing with the cash flow does not affect the government's net return; it merely affects the timing.

Mr Spence—That is right.

Senator MURRAY—If the timing could be dealt with, would that help you considerably?

Mr Spence—Yes.

CHAIR—On behalf of the committee, thank you Mr Spence, Councillor Matheson, Mr Spargo and Ms Hunt for your evidence.

[4.38 p.m.]

DUFTY, Mr Gavin John, Policy Officer, Victorian Council of Social Service

FIFER, Mrs Dimity, Chief Executive Officer, Victorian Council of Social Service

CHAIR—Welcome to the inquiry. The normal form is that you might choose to give an opening statement overviewing your submission and then open yourself to what I suspect will inevitably be a number of questions from the committee.

Mrs Fifer—Thank you. We have an additional one-page sheet which we have called 'RPI Research or Why a GST will need CPR if it doesn't understand RPI!', and a report entitled *What's your inflation rate? Relative Price Indices for Melbourne Households* that we would like to table as extra documentation.

CHAIR—The secretary will collect those from you.

Mrs Fifer—On the assumption that people have worked through our submission, we wanted to give you a quick overview, introduction, to VCOSS and a summary on that one-page sheet, and then draw out some of the major points in our submission. There are a few miscellaneous issues that we have not addressed that you may seek further clarification on.

To begin with, I think it is very important that people understand that while at the beginning of our submission we did say that we were very supportive of submission from ACOSS and the rest of the COSS network nationally, it needs to be identified that the COSS network and ACOSS are not subsets, that we are affiliated members and therefore separate organisations. In terms of organisation, that is fairly important to keep in mind: we are not state offices per se.

In terms of the one-page summary, which we have called 'RPI Research or Why a GST will need CPR if it doesn't understand RPI!', our research that we released in the tabled orange report *What's your inflation rate? Relative Price Indices for Melbourne Households* is certainly a very useful tool, we believe, in helping the Senate committee understand the differential impacts on low income and disadvantaged households across Australia.

So, reading from the sheet, we assert that the consumer price index, the CPI, as we all know, is an average measure of changes in costs of goods and services for only those households that are capital city average wage and salary earners. So, at the very outset, you know that, if you are not a wage and salary earner and you live outside the metropolitan area—meaning capital city—the CPI is not configured to discuss price increases for you. Its use, therefore, is limited when talking about inflationary impacts on different Australian households such as statutory income or rural and regional households. One size does not fit all when using CPI to talk about the cost of living and inflation rates. It is an ongoing concern of ours that something as complex and strategic as a new taxation system unfortunately is still using the CPI in this way.

Moving along, we know that different groups also have different expenditure patterns due to life cycle, for example, youth or aged, and lifestyle, for example, using public transport and public housing as opposed to being a home purchaser with a private car. As we know, the CPI is actually configured more for people who are actually wage and salary earners and who are purchasing their own home. So the weighting is that way.

Our research aims to create more accurate predictors for individual households. We have assessed price changes for particular households' goods and services and the impact this has on the overall purchasing power by factoring in the households' income changes and purchasing patterns. We have called this measurement tool the relative price index, or RPI. As you can see, the methodology is actually creating a more powerful predictor and tool, something that the CPI—which ABS would admit—cannot do.

Using RPI research, we have found that spending power since 1990 shows a decline for some households and an improvement for others. The CPI or rate of inflation averaged over the whole community since 1990 has been 20.4 per cent. When looking at RPI data for the same period, we found that couples with two children purchasing their dwelling and using private transport have an RPI of 18.42 per cent, so their households have in fact the lowest RPI rate, and their inflation is effectively less than the CPI. Good luck to you if you are within that household category.

However, the highest RPI rate over the same period is for households on aged care and disability pensions living in private rental housing and using public transport with an RPI of 34.23 per cent. Their inflation rate is significantly higher than the CPI.

There is no level playing field, VCOSS believes, when discussing the inflation rates experienced by different household types in Australia since 1990. Therefore, for government policy initiatives to be effective and credible, they need to understand and respond to the specificity of individual household impacts when dealing with either policy changes affecting the whole community or for specific households receiving pensions, benefits or concessions.

The federal government's proposals for entering a broad based GST is not entering a level playing field of households across Australia. It is entering an environment where the spending power of certain households has already been significantly reduced through market forces and government policy. By implication, these particular households will continue to be negatively impacted by the proposed across-the-board GST rate on goods and services and the inappropriately, we believe, configured level of compensation. An escalation of disadvantage is likely to occur where the broad based GST and concession proposals do not match the actual spending and income patterns of particular households.

We ask the committee: how can the federal government justify the continued introduction of major policy changes that entrench the experience of disadvantage by particular Australian households? These households, we believe—and we go into more detail in our submission—cannot afford to be any worse off under the proposed taxation changes.

The major point in our submission is that we are looking for a mind-set change akin to the change that happened when people understood that 'poverty traps' was a particular term around effective marginal tax rates. There has been a lot of very creative work done to try to eliminate those poverty traps, but what actually happened first was that there was a mind-set change to understand those. We believe there also needs to be a mind-set change to say that the CPI is an inappropriate tool as an across-the-board indicator in the taxation debate.

In our submission, on page 3, a sentence in the second last paragraph reads:

The Senate committee needs to ascertain how proposed government policy on GST items and compensation packages will not further contribute to increasing financial hardship for these households.

The households that we are having greatest difficulty with are those on disability aged support and unemployment and sole parent benefits.

On page 5 we have extrapolated the actual households who are noticeably to significantly worse off. In our state budget submission we came up with the actual numbers to help the state government configure its concessions.

On page 6 we say:

These disadvantaged groups are already experiencing a disproportionate increase in cost of living and are caught in a poverty trap. Their statutory incomes are being indexed at a rate lower than their particular relative price index.

So it is not a matter of starting now and working out the effect of the GST. It has been happening since 1990, and we need to understand this.

Pages 8 to 9 contain our conclusion and our recommendations. We feel that it is vital to the nation’s future that disadvantaged people are not being penalised by the effects of the highest inflation rate. The CPI, unfortunately, has been bluffing us for too long. We have four recommendations on page 9, and we also want to add there that we ask the committee to give its terms of reference a little rejig to look at the interaction of federal and state taxation systems. We believe there has not been enough research and we are quite happy to do more in this area, if so required. On the differential impacts on low income and whole community, as a federation we need to understand different state impacts of the interaction between federal and state taxation systems and federal and state concessions as well.

The miscellaneous issues I wanted to allude to are issues that we have not been able to ascertain from many inquiries to taxation lines, et cetera. There are some questions on the lifestyle of those experiencing poverty. For example, we have not been able to ascertain exactly what rates of GST will affect those people who need to access pawnshops at different periods of time to gain extra financial assistance. Will the rates of emergency relief and food vouchers, which the government is very committed to, increase? It is a minor issue but one which impacts very much on low income households. Will the four per cent increase on concessions and benefits go also to rental assistance and concessions at federal and state level? We are really seeking some answers on that.

We would also like to put in the idea of the use of a model, either policy or operational, where we actually link GST exempt or free to people, as opposed to goods and services. At the moment, in Canada, in an operational sense, there is a card being trialled by which people like health-cares can go around town and actually become GST exempt, so you link it to the people or the households. We are saying that there is a policy already existing with pharmaceutical goods—I have the data here from Centrelink, faxed through to me today—

which could be a useful model, particularly for disability pensioners. We really need to find a way that the expenditure of people on disability pensions who have high expenditure on goods and services can be capped so that their lifestyles will not be further eroded. Having some sort of mechanism by which, after a certain level of expenditure, they could then be GST exempt, would be a very effective way to help these people. Thank you very much.

CHAIR—Thank you, Mrs Fifer. Does Mr Dufty have anything to add?

Mr Dufty—No, I will wait for the questions.

CHAIR—All right. Before I ask Senator O'Chee to start the questions, I will take the opportunity from the chair to ask a question up front. In your submission you indicate that you are consistent with ACOSS in what you are putting to us. Is that right?

Mrs Fifer—In terms of the ACOSS principles and recommendations, this research, you could say, adds value to the other ACOSS research. They are not presenting RPI research. Our submission is very particular in that respect—we decided to give a lot of depth in the RPI research.

CHAIR—Let me articulate what I understand to be ACOSS's position on a GST, and you tell me if I have got it right or wrong. My understanding is that they are in favour of the principle of a GST, subject to a range of qualifications, most of which appear to be your recommendations 1 to 4. From that point of view, it would seem that ACOSS will be making representations to the government to obtain agreement from it to agree with the qualifications you have put. If the government does not agree, do you support a GST in the form presented to the parliament or not?

Mrs Fifer—That is why I made that recommendation earlier. Ours is a totally separate submission and set of recommendations, so we would like to see ours evaluated on its own merits. We are saying we support the principles of ACOSS in looking after low income and disadvantaged groups, but in terms of some of the recommendations that is really up to you in your report. We are not here to contradict ACOSS. We are saying our research is separate to ACOSS research and we would like it to be seen on its own merits.

We do not support the introduction of a GST as it is currently configured, because we do not believe it has understood the differential impacts low income and disadvantaged households have been experiencing. We believe it is not entering a level playing field and, as such, has been poorly researched and modelled, so we are looking for significant changes. A lot of this is historical data. We are just saying that the government needs to understand that they are using flawed methodology by using the CPI. Much more than that I do not think we are expecting at this stage. That would be a great shift if we could get a win on that one.

CHAIR—I do not want to put words in your mouth, but did I understand you to say that you do not support a GST unless these qualifications you have put down are met?

Mrs Fifer—Yes.

CHAIR—That is truly the case?

Mrs Fifer—Yes, because we believe it would continue the already existing disproportional inflationary rates our research has been showing of low income households since 1990. In our orange report you can actually see the spikes on the graph. Whether looking through the window of individual households or through prices changes in commodities, whether it be housing costs, medical costs, you can see the spikes where certain government policies are inserted, whether at federal or state level—changes in pharmaceutical benefits, changes in local government charges. So, yes, for the integrity of this research, we would have to say a GST should not be implemented. It will have severe harm and impact on low income groups.

CHAIR—We had the St Vincent de Paul Society give evidence to us in Canberra last Thursday. They are a national organisation, they spoke nationally. Is the St Vincent de Paul Society a member of VCOSS?

Mrs Fifer—Yes, it is.

Mr Dufty—Yes.

CHAIR—They characterised a GST to this inquiry as—and I quote them—'un-Australian'. Do you agree with them?

Mrs Fifer—Un-Australian? I wonder if it is unworldly or ununiversal, actually. I would not put a GST in this configuration on any country on the planet, to be fairly honest with you. We do not go into that sort of terminology, Senator Cook.

CHAIR—I think they characterised Australia as an egalitarian country, and justified their description on the basis that it did not meet that test.

Mrs Fifer—To be fair, if we are going to start down that path, we would have to say that this data is showing we are not an egalitarian society. There are some fairly chilling facts and figures that come through on these graphs. The methodology is showing the level of poverty experienced, particularly outside metropolitan areas in Australia, is such that you just cannot hold your head up in any shape or form. That is why people are finding it very difficult to find that, since the Henderson poverty report came out over 20 years ago, levels of poverty are actually increasing. It is really very chilling. When we find that productivity and economic growth of Australia have been increasing, why are certain groups in our community still experiencing such disadvantage? It is not until you get behind the data and look at the world through measurement tools like this that you start unpacking what is happening.

CHAIR—The other point that the St Vincent de Paul Society impressed on our committee is that a characteristic of people who are living in poverty or in straitened circumstances is that they do not have any discretionary income at all—

Mrs Fifer—Yes.

CHAIR—and that any charge, no matter how small, looms for them, in terms of their income, as quite significant. Is that fair?

Mrs Fifer—Yes, definitely. If you talk to any emergency relief agency around Australia, or citizens advice bureaus or whatever, and talk about their day-to-day experience of people on low incomes, particularly a day or two before their pension is due every fortnight, it is really quite harrowing. People do not have the extra dollars to soak up any living increases, and their income is being eroded. That is why we even asked the simple question about food vouchers.

For those of you who know about emergency relief, one interesting example is that often you can get a cheque to be cashed at a bank—it is usually for around $20 to $25. When you take that up to a bank to cash it, they actually charge you $5 to cash that cheque on the spot. So you have already lost $5 out your $20 to feed your family that night—and that is for a whole family's meal. Then you go to the supermarket. If you are living in rural areas, where supermarket costs are far and above what CPI ever measures, you are starting to erode it even more. Understanding the real dollars and the real life experiences of those people who are experiencing true poverty in our community is really what VCOSS and societies like St Vincent de Paul and the rest of the COSS network are trying to illuminate.

CHAIR—You are familiar with the work the St Vincent de Paul Society does. Are they in a position where they are qualified to make these statements, do you think?

Mrs Fifer—Most definitely. Whether it is as a research and a policy arm, or for everyday living experience, yes, those and others like them, like the Brotherhood of St Laurence, are at the coalface of dealing with these very households.

CHAIR—Thank you.

Senator O'CHEE—I suppose most of these questions, because they are fairly technical, probably end up being for Mr Dufty, but I am happy for either of you to answer. I have gone to page 6 of your little orange report. You say in the second paragraph of page 6:

Weightings in this report are derived from data outlined in the ABS HES Household Characteristics—

Mr Dufty—Yes.

Senator O'CHEE—So what have you done to the Household Expenditure Survey data set to construct yours?

Mr Dufty—There is another sheet of paper that has been handed around—the collection of the CPI raw data, groups, subgroups et cetera—which people should have. What you have got is the CPI—that is the goodies in the baskets of goods and services that they go out and regularly collect the prices for—and you will see that it is made of up groups, subgroups and individual items.

The Household Expenditure Survey has the same sorts of goods and services within it. However, it classifies them in different categories. So there needs to be some rejigging between the categories to be able to weight up the CPI data, the raw price rises, into different expenditure patterns, which is a similar methodology to that being used when you are calculating the CPI and also by Melbourne University Applied Economics and Social Research Institute.

Senator O'CHEE—So just what have you done to the data set?

Mr Dufty—Nothing.

Senator O'CHEE—Nothing?

Mr Dufty—Nothing. I have just reallocated them so they match, so the raw data on prices here matches expenditure items within the HES.

Senator FERGUSON—You reallocated them?

Mr Dufty—Yes, which you can do using ABS details.

Senator FERGUSON—Does the ABS approve that sort of methodology?

Mr Dufty—The ABS is aware I am doing it. I have spoken to the person who puts together the CPI data. The ABS does it in calculating the CPI themselves—they reweight them all the time.

Senator FERGUSON—I am not sure why you have moved away from HES data. We are talking about surveys of 8,000 people when we are talking about HES data.

Mr Dufty—It is some particular categories within the quintiles in the HES ABS.

Senator FERGUSON—Let me finish what I was going to say. We used 8,000 people in the household expenditure survey. Professor Harding and others who have appeared before this committee say that once you break those aggregates down and disaggregate then your findings become more and more unreliable the more the disaggregation becomes. You have got to a stage where you are talking about the highest RPI, where you are talking about your RPI rate of the same period for households on aged care, disability pensions, living in public rental housing and using public transport with an RPI of 34 per cent. How many people are you talking about in that category?

Mr Dufty—If you go to the first document that I have got, I think you will find in Victoria it is about 6,100—on page 5 in the shortened version.

Senator O'CHEE—But how many of the household expenditure survey—that is the question?

Mr Dufty—I am unsure, but it would be a low number.

Senator FERGUSON—Have these figures been statistically analysed?

Mr Dufty—My understanding is that the Victorian Treasury is doing that at the moment.

Senator FERGUSON—They are doing that but it has not been done yet?

Mr Dufty—No. I understand the concerns with the household expenditure survey. However, without other data that looks at different expenditure patterns from different household groups, using the CPI, which is an average on a distribution curve, a bell shape curve, does not look at the margins. The margins are really important and are for the community, I believe.

Senator FERGUSON—What is your margin of error?

Mr Dufty—We do not know. We do not even know the margin of error within the HES data in some quintiles either. There is not the data set—we are using the best that is available.

Senator FERGUSON—I think we do know the margin of error in HES.

Mrs Fifer—I think we have to remember, too, that there are two issues here: one is the data sets and the other is the methodology of creating the RPI. We are more than happy for ABS to smarten up their act and give us more accurate HES data, but we need to understand that we are not just talking about data sets, we are also talking about the methodology of using the data sets—and that is the important one.

At the moment the CPI is being used and it is a very blunt instrument. Australia needs a better tool as an indicator, and the methodology that we are presenting to you is a separate and adjunct issue to the data sets. So when the methodology is being ticked off, we are looking for more and more improvement with the data sets over time. Gavin is continually reconfiguring every time new data sets come through.

As you will see in our state budget submission, we are presenting this now to governments in terms of their work with state budget submissions and federal government submissions. Government departments are saying to us, ‘Yes, we have not liked having to use CPI—whether it is to look at education costs, housing costs or the rest of it.’ People are looking for a powerful tool like this. So the methodology is there. Yes, there is a margin of error but even with a margin of error of whatever per cent you might like to choose, it is still showing up—

Senator FERGUSON—We do not want to choose it. We just want to know what it is.

Mr Dufty—We do not know.

Senator FERGUSON—It could be a 50 per cent margin of error—you would have no idea?

Mr Dufty—It could be—we do not know. But what it is indicating is that there is a difference there. If people are serious about working out what different inflation rates or pricing indices for different groups are, the best minds in Canberra can do that very quickly, I believe, up at the ABS.

Senator FERGUSON—We have got universally accepted recognition of the CPI index and we have other recognition of the household expenditure survey, which is done by a separate group but using large numbers. You are saying that we should disregard those and only use your survey, which you feel is far more accurate?

Mr Dufty—I am not saying to disregard them at all. I am saying that they are not the full picture. When you calculate a CPI based on wage and salary earners in the metropolitan area you discount 30 per cent of Victorians instantly because they are statutory income holders. You discount all of the people that do not live in the metropolitan area regarding what their experiences are and what their costs are. That, in itself, I believe, certainly raises concern for me. It is not actually mirroring the experience that our members and our other surveys of emergency relief agencies are showing. That is where the impetus for this came from.

Senator FERGUSON—I will read you a quote because you are talking about reliability of existing models and existing surveys. It talks about distributional impacts; it is a research paper done for this specific piece of legislation.

I will just quote, as I have quoted it to St Vincent de Paul:

One of the issues raised for discussion during the review concerned a study undertaken by the ABS in 1992 (ABS 1992a) and updated in ABS (1993) and Higgins (1995) which showed that an experimental index constructed to reflect the quite different expenditure patterns of age pensioner households displayed little variation from the CPI over an extended period of time (0.1 index points over 11 years). There were, however, differences in index movements when shorter periods were examined.

So in fact you have got this review that has taken into account, over a long period of time, the CPI varying very little when you are talking about household expenditure patterns of aged pensioners to use one group. Once you get down into smaller groups or once you disaggregate or once you use shorter periods, then it is only natural that the statistics that you come up with can vary a great deal from those that are taken over a different pattern by agreed methods of statistical analysis.

Mr Dufty—I agree. I do not disagree with you. What we are presenting here is looking in the rear vision mirror since 1990 and saying people consume things differently, which they do. A person in public housing will not be purchasing a home; they are in public housing. If you go to the raw data sets in the CPI and look at the public housing costs, they have risen by about 35 per cent whereas home ownership costs have reduced by 25 per cent. If housing makes up, let us just say, 15 per cent of people's expenditure, that has got to be a huge impact. Those are sorts of raw data regardless of how you weight it, which is why I presented this data here. People cannot use public transport as well as drive a car at the same time. Some people cannot drive a car and they are bound in public transport. Public transport costs again have gone up where private motoring costs have risen at about the cost of inflation.

What we are saying is that people do not have life choices in all cases. If they are in public housing, they are in public housing. If they using public transport, they are using public transport. It is those margins past the first deviations in the standard distribution curve, which is where the impacts are and which is where the people are going to get burnt.

I do not disagree about the averages being good. Once you start to step out on the edges of the bell shape curve, that is where the hurt is. What we are trying to do here is just say, ‘Hey, we think, given all the methodological issues, that we need to look out here from our previous experience.’

Senator O’CHEE—That is exactly what we are trying to examine, which is the accuracy of what you are talking about. You already concede that you do not know what the margin of error is but let us leave that to one side. You have told us that you just took the entirety of a household expenditure survey data set. You reallocated it but you have kept the entirety of the household expenditure data set.

Mr Dufty—We have kept the broad categories within the household expenditure survey and then looked at particular income groups or quintiles within those income groups to actually represent a household type because I have no other data to do that.

Senator O’CHEE—But you did not exclude anybody from the household expenditure survey data set? Before you allocated them to different groups, you did not go through the data set and exclude anything?

Mr Dufty—Not that I am aware of.

Senator O’CHEE—The problem that I have with accepting what you say is that Peter Dixon told us in Canberra that when he went through the household expenditure survey data set, he excluded 680 out of 8,600 households because he said data was so wildly inaccurate as to not be worthy of inclusion. You have included that data.

Mr Dufty—Yes, there are problems with the data sets. I do not dispute that. What I am saying is that the CPI is calculated based on a particular household. That assumes that they only consume a tiny proportion of public housing cost for example, whereas we know people in public housing, all their housing costs—

Senator O’CHEE—We accept that there may be differences. We are not arguing about that. You have come here with a set of data and you are saying, ‘Look at what I am saying to you because I have done this statistical survey.’ What I am saying to you is ‘How accurate is your statistical survey?’ when you admit that you do not know what the margin of error is and you are now admitting that you have not actually gone through the data set to look for households whose dissavings rates every other modeller who has come before this committee has said are so wildly inaccurate as to not be worthy of inclusion.

Mr Dufty—I agree. I am using the data that is provided by the Australian Bureau of Statistics through the household expenditure survey. That is the best data that I can get hold of and that is what we have used. Yes, there are problems with it. But it is indicative. It is looking at issues. That’s all. I agree with you.

Senator O’CHEE—The problem is that the other modellers have said to us that there are very good reasons for excluding many of those. For example, the 680 households that Peter Dixon excluded were excluded because they had dissavings rates of 300 to 400 per cent. I think you would accept the fact that nobody could dissave at 300 to 400 per cent over any length of time.

Mr Dufty—I agree, and I know the problems of the household expenditure survey. I do not disagree with you.

Senator O'CHEE—The 680 that have been excluded would constitute a fair proportion of the people that you would be using for your RPI.

Mr Dufty—We do not know which particular categories the 600 are in. It may or may not have. But I assume you are right.

Senator O'CHEE—You are concerned about groups that dissave. He said he excluded 680 households that dissaved out of the Australia-wide total of 8,600.

Mr Dufty—About five per cent, yes.

Senator O'CHEE—Yes. But it is not five per cent of the dissavers—it was a very large proportion of the dissavers. He said that was because he just could not believe it. He said one of the reasons is that people will generally tell you what they are spending but not what their income is.

Mr Dufty—And if you have a look at what I have done, you will see that I have only based the relative pricing indices on expenditure, not on income.

Senator O'CHEE—The question is that if you say, 'All right, these people have this expenditure problem'—

Mr Dufty—Yes.

Senator O'CHEE—And if the problem is only a problem when it is relative to their income—

Mr Dufty—Yes.

Senator O'CHEE—Then you cannot exclude the income aspect. That is what Peter Dixon said.

Mr Dufty—No, and I am not saying that. What I am saying is this: for the graph I have assumed that the income level was adequate in 1990 and that pensions and benefits are indexed at CPI. So the income level I am assuming is the CPI line, and the expenditure is their RPI line. That is all. I am not looking at income at all, just purely household expenditure, which will be 100 per cent—which does not take in dissavings, on one hand, but on the other hand does not take in savings either. It is just an expenditure line, which is similar to the CPI methodology.

Senator O'CHEE—But if other modellers do not think that that is an accurate way to construct a data set which you are then going to use to model the tax change—

Mr Dufty—Because of the income.

Senator O'CHEE—Why should we believe you?

Mr Dufty—I am not asking you to believe me. We are putting information here that we believe will be of benefit to the Senate, to inform the debate and get a better outcome for all of us, because that is what I think we are here for.

Senator O'CHEE—I have a final couple of questions. You have gone and done this; let us leave all the other discussion we have to one side. What has this told you about changes in tax rates and, in particular, the GST? I understand the argument you are making. My question to you is: have you used your data set to model, first, the removal of sales tax, and, second, the imposition of GST?

Mr Dufty—No, but Melbourne university has. What we can say it indicates is that when people say, 'Compensation is adequate' they are looking at the average—the middle of a bell-shaped curve. There will be people on the margins that will be real winners and there will be people that may be real losers. What we believe this research is doing is indicating who are likely to be the real losers, just because they are consuming certain goods and services exclusively or at different rates than others. That then allows us to develop methods and processes by which we can alleviate or ameliorate those problems.

Senator O'CHEE—You are not querying the government's desire to ensure that people who are vulnerable are compensated? You accept that the government is trying to do that? Your quibble—

Mr Dufty—I personally do, yes.

Senator O'CHEE—That is fine.

Mr Dufty—I am saying that it is about the margins.

Senator O'CHEE—Thank you.

CHAIR—It is about whether it can be done adequately?

Mr Dufty—Yes.

Mrs Fifer—Can we just confirm, though, that it is the methodology we are talking about. In terms of the footnote here, this is the first time someone has come up with a tool that looks at the matrix of the three things—a tool that gives the relativity between the changes and the costs of goods and services, their particular expenditure patterns, and the changes in their income level. It is the methodology that we are asking you to take on board, and the use of that in your deliberations.

Whether you believe Peter Dixon over VCOSS is your decision. We can give you more data and configurations; that is not a problem to us. We are just saying: if you did take this to be true, what would it say to you? What then does the federal government need to do to ensure that its modelling is extremely accurate and does not—if this is true—actually increase disadvantage in our community?

Senator FERGUSON—You are asking us to accept your methodology when in fact we are not experts on what is the correct methodology. It would need to be approved by somebody else.

Mrs Fifer—Yes. But it could be that you say, 'We believe research is needed to ascertain if this methodology will actually help us to make a decision on a taxation system that will have such huge ramifications for our community, because if it is true, then we do have low income groups that will be severely impacted.' There are others, of course, who do take it on board—Productivity Commission notwithstanding—who will be doing research on this. So take that as it is.

CHAIR—Yes. In fact today we have had, from business groups in the main, an argument about an efficiency issue. We are having, from you, an argument about a fairness issue. It may well depend on to what extent various members of this committee weight those as important features of the tax system.

Mrs Fifer—Yes.

Senator MURRAY—I think your central proposition is that of the government's, and it is twofold: firstly, that in relative terms the situation of the poor, vis-a-vis that of the well-off, has deteriorated over the long term; and, secondly, that in absolute terms the poor have had a decline in real disposable income and in living standards. Is that correct?

Mr Dufty—Could I put that more accurately? It is a decline in purchasing power: the dollars in their pockets are buying less. It is not to say they do not have more in their pockets in terms of income. It is about purchasing power.

Senator MURRAY—So that is a third proposition. The government have agreed with all that because they have sought to attack the problems of the poverty trap, to attack the problems with income tax levels and to provide compensation for the tax changes. So if the intent of the government accords with your approach, then the real life experience of your organisations, compared to the Treasury statistical assessment of your situation, matters. That is what you are saying?

Mrs Fifer—Yes. Also, as you say, the government, by putting forward a compensation package, both in dollar terms and in terms of percentage increases, is admitting there are going to be differential impacts and they want people to be compensated. We are saying: let us be more accurate and a lot more specific and particular about the sorts of tools you are using to configure those increases.

Senator MURRAY—Let me pursue this a little further. The Prime Minister has said, as a generic, general proposition for Australian people, that his package should make no-one worse off. Would you agree that only the mean and the hard-hearted would seek not to make the poor better off? In other words, the proposition I am putting to you is that whilst for the mass of Australians it might be satisfactory to say no-one should be worse off, for some individuals, such as tax avoiders, tax dodgers, black economy people et cetera, you want them to be worse off; and for the poor, surely we want them to be better off. Would you agree with that proposition?

Mrs Fifer—I guess here we are getting into the debate between equity and equality types of issues and changes. We can get back to you on that if you want our considered opinion; we have not gone down that road here. That is a huge issue: do you reconfigure the winners and losers? What we are saying is that we do not want a maintenance of the continuing situation, that we do not believe it is a level playing field at the moment, that by entering a GST you will just maintain people's relative status. We believe that the status of low income and disadvantaged groups—and we are being consistent with our research data—is actually getting worse. The disparity is increasing at the moment.

Senator MURRAY—What I am putting to you is absolutely central, because this committee will have to decide on the level of compensation which is appropriate for each cameo—and I distinguish between the poor and the low income, incidentally. If it is your proposition that, because of what has happened in Australia over the last 25 years and maybe longer, the position of the poor has deteriorated, both in relative and in absolute terms, then I would suggest to you that one of the considerations of the committee ought to be to make the poor better off. If that proposition was accepted by the committee, it requires a substantial shift from a view that people should be no worse off. That is why I put that to you.

Mrs Fifer—Okay. You need other data and methodology as well, whether it is the Henderson poverty line or other aspects of looking at poverty issues. Certainly we do not just use RPI data; we look at emergency release surveys, et cetera. There are a number of different ways of viewing the life of those people living in poverty.

You make a very good point, Senator Murray. It is a huge issue that you are facing. We are coming to you today to say that, in making those decisions, we are seeking that you will ensure that the methodology for creating those numbers is an accurate one. So if you are going to talk about certain households, we are saying, 'Can you please talk about them appropriately and relevantly.' If you are going to talk about people who are on a disability pension, who have not much hope in the world of ever getting another job again, et cetera, can you please use data, numbers and percentages that relate to their real lives. That is what we are asking.

Senator MURRAY—All right. Now let us move on from there, because this is the important point: the government senators have correctly made the point, and Mr Dufty has correctly made the point, that the data available at this lower end is very difficult to compute. Senator O'Chee correctly made the point that 680 households are excluded by one of the country's top modellers. Of course, the reverse of that is 7,920 were accepted as very valid. The second point you made, though not explicitly and I will make it for you, is that the only data we have got for rural and regional Australia is HES, because the CPI attaches to the capital cities, so we have to rely on HES.

Given that the committee, the government senators and Mr Dufty accept the difficulties with HES, surely, if it is dangerous and the margin of error can therefore be wildly varying, and the marginal cost to the individual is massive if you make an error—they cannot buy food; they cannot pay for the housing and so on—you have to ensure that your cushion is greater where the statistical evidence is weaker.

Mrs Fifer—Yes; it is a risk management issue.

Senator MURRAY—Exactly. Is it your judgment, based on what you have seen of the ANTS package, that the cushion for the poor and the low income is too small and too tight, based on what you have received to date?

Mrs Fifer—To be consistent with our research, we would say yes. We are dealing with a vulnerable set of households, vulnerable community members. Yes, we believe that, in terms of risk management, the compensation that is being offered at this stage is inappropriate. And the thing is these data sets are already being used on the Australian community in government policy decisions.

If the greatest thing you can come up with from this committee is to throw out these data sets and say, 'Guys, you come back with some better sets, thank you very much, because we have been suffering'—though 'suffering' may be too strong a word—then that may be the best thing we can get out of it at the moment—and I am not being facetious here. If you want us to reconfigure, taking out those particular households, we will do that as well. We are not trying to be facetious. We are just saying there needs to be a better way to accurately predict the impact of this new system. A few extra months, or whatever it might be, to reconfigure it is not going to be such a bad idea in the long term.

Senator MURRAY—Let me move on to page 9 of your paper, recommendation No. 3:

> A change in the nature and range of items attracting a GST, including the zero rating of food, because of the need to significantly increase concessional arrangements to avoid the continuing loss of purchasing power of low income households as determined by RPI.

The business organisations we have heard evidence from so far say that they do not quarrel with the compensation approach, although a number of them think it is adequate already, which we could disagree with. They accept the compensation approach. They do not accept zero rating food because they maintain it will increase complexity and compliance costs for those businesses which have to deal with it. Why would you argue for the zero rating of food rather than increased compensation?

Mrs Fifer—I guess it is a matrix response, and, for the zero rating of food, unless Gavin has any other comments here, I would be going to the ACOSS research on that, so we have not done any detailed modelling. Though certainly, again, because we know the high levels of expenditure patterns in terms of the weighting of food in low income people's lives, we believe it is an area that we really need to take seriously, and also, again, because of the metropolitan data of CPI. Certainly, there is differential food pricing between states and between metropolitan and rural areas, let alone Aboriginal communities, who do not perhaps suffer at $3 a kilogram for tomatoes but $3 per tomato. So this is an issue that we still want to take seriously, but as to the zero rating of food, I guess I would ask the committee to go to the ACOSS research.

Senator MURRAY—Isn’t it true that one of the reasons that you want food zero rated is because, within the statistical data, the expenditure on food is far more certain and well-established statistically and understood than is, say, the amount of income people get, or expenditure on alcohol, or other of those areas. Therefore, you know the consequences of zero rating food, whereas you do not know the consequences of lifting compensation by a dollar.

Mrs Fifer—I would agree with you, Senator Murray, and, again, I do not think it is appropriate for us to answer these because the modellings come through ACOSS. However, one thing that I think we do need to make clear about our research is that a lot of what we are trying to put forward is the cumulative effect of price increases over a number of different commodity areas. That has been the real surprise for us as we have come forward with this.

It is not just a matter of saying, ‘Well, what are the price increases in public transport, housing, this, that and the other?’ With certain households, the way that their expenditure patterns reflect their lifestyle and life cycle, it is the cumulative price increases over time.

We have these discussions with government departments all the time who do their departmental concessions and budgeting, perhaps in housing, and go, ‘Well, we are okay; our concessions on housing work.’ Then you toddle off to the education department or community services, and people are not understanding that people live their lives across government portfolios. So another mind shift change that we are hoping to put forward is that it is the cumulative impact. Can you see the point that I am trying to make there? That is another area that I think we really need to understand. It is the cumulative impact of price increases on all these areas that take up all the dollars of a low income household.

Senator MURRAY—That is all I have, Mr Chairman.

Senator CONROY—I just want to come back to some comments you made a little earlier in your presentation when you were talking about the modelling. We have been engaged in a healthy debate, even as recently as a couple of moments ago, about the modelling that we want done. We were talking about the inflation figure and what number to plug into our model that we are having designed for us. You were saying that if somebody modelled—us, for instance—without using your RPI figure, it would be poorly researched and not good modelling. I think you said earlier ‘poorly researched and poorly modelled’?

Mrs Fifer—Sorry, if you just use straight CPI data?

Senator CONROY—Yes.

Mrs Fifer—Yes, because it is a blunt instrument that does not measure the three aspects that the RPI seeks to. If you come up with another tool, that is fine by us.

Senator CONROY—So you would say to us, in terms of the debate that we are having among the committee members, that it is very important that we do not just—

Mrs Fifer—Yes. It is partly a process recommendation on our behalf.

Mr Dufty—Do not dress everybody in the same clothes is, I suppose, a simple way of putting it.

Senator FERGUSON—Even though it has been shown that over a longer period—

Senator CONROY—An excellent way to dress. Over 11 years or so, maybe you would wear the same clothes—I do not know.

Mr Dufty—Some people do.

Senator CONROY—My concern—and you have come before us saying that you support the ACOSS position—is that ACOSS has not taken any notice of you.

Mrs Fifer—The ACOSS principles. Don't forget, we are not subsets of ACOSS. We all give different bits of information that add value to each other. So it is a collaborative cooperation here. So you will see something from us—

Senator CONROY—But ACOSS's modelling has not used your methodology?

Mrs Fifer—Yes.

Senator CONROY—Therefore, to be consistent, your position would be that their modelling is poorly researched and poorly modelled?

Mrs Fifer—I think they are using their research quite appropriately, but we are coming from a different angle again, and you need our research to be consistent.

Mr Dufty—ACOSS's modelling is fine in looking at an average. The margins is what we are bringing to the table here. It is the shape of the overall curve.

Senator CONROY—Why haven't ACOSS adopted your methodology?

Mr Dufty—They probably did not ask Melbourne University to do it that way. Ask Mr Raper.

Mrs Fifer—We are not subsets, or report to each other. We all know each—

Senator CONROY—No, but you are coming forward, and in the front of your submission you say, 'We support ACOSS's position.'

Mrs Fifer—Yes.

Senator CONROY—I will come to ACOSS's position in a minute because I just want to clarify whether your position is supporting ACOSS's position or not, given that you are not a subset.

Mrs Fifer—It is really the broad principles. I understand what you are trying to say. I did not want to make any difficulties with that sentence.

Senator CONROY—In terms of this morning's newspaper—I am sure you got up and enjoyed them as much as I did, but probably not as much as Senator Ferguson—the heading says, 'GST a winner for poor welfare group.' It says, 'Low income earners and the poor will be better off under the Howard government's GST package, according to a confidential analysis by a leading welfare group, ACOSS.' Do you agree with that?

Mrs Fifer—No, but I think you need to go to ACOSS and discuss that, and also to the journalist. It is not a battle we are here to—

Senator CONROY—It says, 'ACOSS has not been able to prove that any household will be worse off.'

Mr Dufty—I think the key question to ask ACOSS, or the people who did the modelling—again, they looked at average unemployed people—is what happens if they live in public housing? How does that change? They have weighted their unemployed person and are saying some of them are similar to the way the CPI is weighted. It is when you actually start to prescribe certain goods and services, which you can for certain groups, that it actually starts to change the shape of the curve. You get garbage in, garbage out with data. That is what happens. I am not saying it is garbage, but they have gone in and said, 'This is the average. What is happening to the average? The average is better off.' Or, 'We thought the compensation packages are adequate.' If we have, say, in Victoria, 180,000 aged pensioners, it is adequate by half a per cent or whatever it is.

Senator CONROY—We have a choice, and quite literally this debate has been taking place around you as you have been giving your submission about what numbers we plug in—the garbage in, garbage out argument. We have been having that very debate here about what numbers to plug into the model. Why haven't ACOSS plugged in your numbers to their model? It is their model. They have commissioned the research. Why haven't they used your methodology?

Mr Dufty—I do not know. You will have to ask ACOSS.

Senator FERGUSON—We will find out on Thursday.

Mr Dufty—I am looking forward to it.

Senator CONROY—And the question to ask them is why didn't they prescribe people who use public transport solely or public housing solely. I do not know the answer to that.

Mrs Fifer—I think at this point—I do not know if it is in the media's interest or whose interest it is to create little bun fights around the edges between different players—

Senator CONROY—This one is not around the edge. This is the most fundamental argument that the committee is facing.

Mrs Fifer—Yes. What more do you need from us in terms of this particular issue? Obviously, you are trying to differentiate, yourselves, between whether it is data sets or methodology or what have you. We are willing to help out in any way that we can. And yes, it is recently released research. And yes, productivity commissions and Treasury and finance departments around the country are looking at this to say, ‘Is this the new tool or not?’ So we acknowledge that we are presenting this, and it is probably fortuitous in the light of the taxation debate, but it might be too early for you. What more do you need to assist you in your decisions?

Senator CONROY—Certainly, from my perspective, I would be interested in seeing how your numbers plugged into the ACOSS model. The difference between the ACOSS model and the Melbourne Institute model, the Dixon model, the Econtech model, it has been generally agreed, shows not that much of a variation between them all. The question is what numbers you plug in. I would certainly be interested if you were able to convince ACOSS to commission your numbers being plugged into—

Mrs Fifer—Sure, and we discuss things with the team at the Melbourne institute.

Mr Dufty—They are all plugging in the same average. They are saying, ‘This is the average,’ and they are not actually specifying, which is what makes this different. If you do specify particular types of consumption of goods and service, you then start to see the margins on the curve.

Mrs Fifer—And then you can make more intelligent decisions and gain better leverage points. We all know there are only certain dollars in the pie and all the rest of it, but if you understand where the leverage points are you can make more intelligent decisions of where the best concessions or the best rates may be.

Mr Dufty—The other thing you can do when you start to do that—and it needs to be refined and, yes, there are a whole lot of questions—is to actually have different compensation packages for different groups, because you better understand where the groups are, where they have come from and their expenditure patterns. I know that adds complexity and that everybody freaks about complexity.

Senator CONROY—Again, this morning’s newspaper report says that ACOSS says in its submission that it does not claim that low income households will be worse off as a result of the tax package. You would not be able to agree with that based on the data that you have configured?

Mrs Fifer—No, and I do not know that ACOSS is saying that either, because Michael Raper very quickly got on the radio and refuted all of that.

Senator SHERRY—There are a couple of points that I would like to pursue. You have referred to people at the margin. Just to get some idea of how many people we are talking about, I have looked at page 5 of your document, and in Table 3.1 you have five columns headed from ‘Significantly better off’ to ‘Significantly worse off’. From my approximate total, just under 800,000 people in Victoria are identified as being ‘Noticeably worse off’ and ‘Significantly worse off.’

Mr Dufty—They are income units rather than individuals.

Senator SHERRY—Okay, income units. We have maybe 1.9 million who are identified as being ‘Significantly better off’ to ‘Marginal change.’ From my calculations, the number of households who are identified as being noticeably worse off to significantly worse off is about 29 per cent. We are talking about three out of 10 Victorians, aren’t we.

Mr Dufty—Yes.

Senator SHERRY—We are not talking about insignificant numbers of people at the margins.

Mr Dufty—No.

Senator SHERRY—Did I understand you to say earlier that in regional areas this type of analysis would produce figures that are worse than this?

Mr Dufty—Yes. If you look at the ABS income distribution data comparing non-metro income distribution with metro income, you will find there are more health care cardholders in the non-metro areas, and you will also find there are a number of lower income groups in those areas. If their expenditure patterns are consistent, you will find that they will be worse off.

Senator SHERRY—If I were to ask ACOSS in my home state of Tasmania, which has a different set of demographics, my assumption would be that it would be actually worse than three out of 10. But that is something for them to pursue.

Can I just put a scenario to you. Let us assume for the moment that the changes you have requested to the package that we are considering are passed in the Senate. I think it is not an unreasonable expectation that over the next few years economic growth will drop, that we may go into a recession and that we will not always maintain the current growth rate. If the budget goes into deficit and the government of the day decides to put the budget back into surplus, either through a combination of expenditure cuts or tax increases, who do you think is going to be hurt the most in that process?

Mr Dufty—That will be a decision that governments make.

Senator SHERRY—I know that, but in your judgment who do you think is going to be hurt the most in that process?

Mr Dufty—If revenue falls, you have to reduce expenditure. It is like a household budget.

Senator SHERRY—But who do you think will be hurt the most in that scenario?

Mr Dufty—The people who use the expenditure, which is most likely to be the people that are reliant on the social security system.

Senator SHERRY—That then leads me to ask: even if the sorts of things you are seeking are varied in the package in the Senate, how do you lock that in to secure the position of the people that you represent?

Mr Dufty—You have a relative pricing index for each statutory income group. Age pensions are indexed to weekly earnings. But you start to get more sophisticated about indexing for other particular groups—that is a suggestion: I have not gone into the detail but you would have an RPI for them.

Senator SHERRY—Do you accept that that is very difficult to do?

Mr Dufty—Complex.

Senator FERGUSON—You asked earlier about what you could do to help us or help us make a decision based on the evidence before us. In relation to the statistical work you have done on the surveys and the data you provided to us, I would suggest that perhaps you get an independent statistical analysis done of your data. Firstly, it would be to find out the margin of error, because there is not much point in plugging your figures into the ACOSS model or doing modelling unless we know what the margin of error is and unless it has had an independent, statistical analysis done which would give it credibility if the information in the database you have used is right. I think that is one thing that you could do, since you asked what you could do to help. Before you go any further, that needs to be done. You cannot take the risk of an enormous margin of error, which you say you cannot guarantee is not in your figures.

Secondly, I want to follow on from Senator Murray’s question when he said that not only does he want to make sure that nobody is worse off under this package, he actually wants the poor to be better off. The government, in coming to the decision on the package in its totality, and using the figures which they believed were the best available to them, did just that. They guaranteed that the compensation package would be 1.5 per cent higher than the CPI, and, rightly or wrongly, they used the CPI as that basis, because the government wanted to make sure that poorer people would be better off than they are now.

Your argument is, of course, that the statistics—or the data, the information available—has not allowed a big enough cushion or does not cover special instances of households. If you could be satisfied that people on low incomes were in fact going to be better off under the package, which would include a GST on food because the government has said that unless the GST remains on food it will reject the whole of the package, would you support it? If the option left to you is to have people on low incomes better off, or marginally better off, or leave them exactly as they are today with the current tax system, and all that is wrong with it, and if you could be satisfied that, with compensation, they would be better off than having the whole package rejected, would you support it?

Mrs Fifer—That is an interesting question.

Senator FERGUSON—It is one we may come to.

Mrs Fifer—Yes, I know exactly, and I am not being facetious in my answer, either. I guess answering one question, when we are trying to say there is a matrix of issues that impact upon this, actually makes it very difficult for me to give you a yes or no answer. We are saying it is an issue of whether you have configured your predicting tools appropriately, whether you have looked at the interaction between state and federal taxes and whether you are looking at ongoing monitoring and indexation. I am not sure that, in fairness, it is appropriate to answer a question about one of those parameters. So, Senator Ferguson, I know you want us to draw the line on that but we may have to get back to you on that. Sometimes we can say yes or no. I think, for that one, we are presenting a matrix of interacting factors and to draw one thread out and say, ‘Give us an answer on that,’ and make a statement on the whole, would be a little inappropriate, but I am prepared to come back to you on that.

Senator FERGUSON—If you could, because it may be the question that we finally have to decide. Senator Murray said earlier that he wants the poor to be better off. I think it is a general view that everybody would like to make sure that people on low incomes would be better off. We have different views as to how we should do it and the level of compensation required in all of those things, but nobody wants to make people on low incomes worse off. It is just a matter of what figures we choose within the whole range of the package to do it. We may come to the situation where we have to decide whether we are going to actually make the lower income people better off than they are today—even if it is only marginally—or we may have the situation where the package may be rejected and they will be in exactly the same position they are in today.

Mrs Fifer—Yes. Or will both of those actually entrench the disadvantaged and increase disparity. That is the interesting thing in our research: notwithstanding whether you agree with it or not, what we are saying is that we do not have a level playing field at the moment. Current policy settings are actually increasing that disparity and increasing the poverty traps. So even if you do insert a level of compensation that might cushion, if you maintain it at that level and do not change some of the tools that you use, saying ‘So what’ is being facetious because, of course, if I could get people $20 a week more I know it would actually help them, but, over the long-term, we are asking for more fundamental structural change in how these policy settings are configured.

Mr Dufty—I think it would have been wonderful had we had this debate back in 1990 because then governments of all persuasions would not have been forced into a position of doing certain sorts of things that have accumulated over time, and now we look from here.

Senator FERGUSON—We could have had it in 1985 but, unfortunately, only the Labor Party had it.

CHAIR—The community had it. Senator Ferguson has put to you a proposition which you have answered but which requires the government not to heed the voice of the parliament, and for the government to remain intransigent with the parliament and refuse then to revisit the whole concept. You could say to the government, couldn’t you, ‘We’ll call your bluff. The whole package is not acceptable; go back and work out something that is acceptable.’ That is another alternative, isn’t it?

Mrs Fifer—Yes.

CHAIR—I just did not want you to feel that you are locked in to only the two questions that were presented to you.

Mr Dufty—That is a bluff.

CHAIR—Well, it is a bluff.

Mrs Fifer—Yes. All of you, whether in the House of Representatives or the Senate, have been voted in to fulfil the particular role that you now stand in. It is not an easy role; it is a very difficult role. But, in terms of the review process, you have to be consistent with the role that the people of Australia have voted you into.

CHAIR—I know what the people of Australia voted me in to do. I stood at the last election on a particular platform. However, I am on a Senate committee inquiring more deeply into the problem.

Mrs Fifer—I guess I mean in terms of your function. You have been voted in as a senator looking at review-type issues, which is quite appropriate in our constitution.

CHAIR—Yes.

Mrs Fifer—So if you say, 'Take it back to the House of Representatives; redo it. It is not good enough,' that is quite appropriate.

CHAIR—That is quite an appropriate thing for the Senate to say. It is getting to the fag end of a long day. We could get into a debate about this. But, in essence, if the government said, 'Rather than make a real change, we will make a slight change. If you do not accept that, you will get nothing,' that is hardly a benevolent government. Anyway, that is probably a debating point that you might hear from me in parliament at some time in the future. I think we are out of questions.

Mrs Fifer—Senator Cook, can I just remind the committee, in terms of that last one—which is not just a throwaway suggestion—of looking at the possibility of expenditure for those people on very high expenditure needs—for example, those on disability support pensions—that some expenditure capping-type mechanism should be created like with pharmaceutical benefits. For example, with pharmaceuticals, you spend so much a year; then, after that, you do not have to pay the co-payments. For people suffering disability, even to change a light globe, everything they do, will attract a GST unless it has been rated as a health service or what have you. So, if it goes ahead, we need a very creative way to protect the lives of those people.

CHAIR—Thank you both very much. That concludes today's hearing. We will resume at 9 a.m. tomorrow.

Committee adjourned at 5.49 p.m.