



COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## SENATE

SELECT COMMITTEE ON A NEW TAX SYSTEM

**Reference: A new tax system**

TUESDAY, 2 MARCH 1999

BRISBANE

BY AUTHORITY OF THE SENATE

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**SENATE**  
**SELECT COMMITTEE ON A NEW TAX SYSTEM**

**Tuesday, 2 March 1999**

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

**Substitute members:** Senators Brownhill, Chapman or Watson for Senators Ferguson, Gibson or O'Chee; Senators George Campbell, Mackay or Murphy for Senators Cook, Conroy or Sherry; Senator Bartlett for Senator Murray

**Participating members:** Senators Brown, Colston, Harradine and Margetts

**Senators in attendance:** Senators Bartlett, Conroy, Cook, Ferguson, Gibson, Harradine, Mackay, 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	<p>The impacts of the Government's taxation reform legislation proposals on the living standards of Australian households (especially those on low incomes), including:</p> <ul style="list-style-type: none"> <li>(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 <i>bona fide</i> charities;</li> <li>(b) a detailed examination of the zero-rating of health services, including an examination of which services should be zero-rated;</li> <li>(c) the effects on community sector organisations of changes to their tax exempt status, and of the compliance costs of the proposed tax arrangements;</li> </ul>

	<ul style="list-style-type: none"> <li>(d) the effects of the proposed private health insurance rebate;</li> <li>(e) the effects on people with disabilities;</li> <li>(f) the effects on public, community and private housing, including the levels of rents; and</li> <li>(g) options for amendments to improve the fairness or efficiency of the proposed legislation.</li> </ul>
<p>Employment, Workplace Relations, Small Business and Education</p>	<p>The employment incentive and education impacts of the Government's taxation reform legislation proposals, including:</p> <ul style="list-style-type: none"> <li>(a) the scope and effectiveness of the proposed zero-rating arrangements for education in maintaining its quality, accessibility and affordability;</li> <li>(b) the effects on employment;</li> <li>(c) the effects of the proposed GST treatment on the quality, accessibility and affordability of employment services;</li> <li>(d) the effects on education of imposing a GST on, or zero-rating or exempting books and associated education resources;</li> <li>(e) the effects on education of imposing a GST on ancillary resources, services and commercial activities, including the effects on overseas students;</li> <li>(f) the effects of the proposed changes to the tax system on employment;</li> <li>(g) the effects on wage costs, particularly if the basic necessities of life are taxed;</li> <li>(h) the scope and effectiveness of changing the unemployment benefits, pensions and Newstart Allowance 'tapers';</li> <li>(i) the effects of the proposed changes to the tax system on training and adult education; and</li> <li>(j) options for amendments to improve the fairness or efficiency of the proposed legislation.</li> </ul>
<p>Environment, Communications, Information Technology and the Arts</p>	<p>The broad effects of the Government's taxation reform legislation proposals on the environment, the arts and information technology, including:</p>

- (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

<b>BRICKNELL, Mr Raymond Leo, National President, Australian Investors Association</b> .....	<b>1347</b>
<b>ELLIOTT, Mr Philip Gregory, Chief Executive Officer, National Credit Union Association Inc.</b> .....	<b>1360</b>
<b>FUNNELL, Mr Geoffrey Robert, Vice-President, Australian Investors Association</b>	<b>1347</b>
<b>GROVE, Mr Basil William, Committee Member, Australian Coalition for Economic Justice</b> .....	<b>1432</b>
<b>HALMARICK, Mr John Edward, Corporate Affairs Director, United Distillers and Vintners (Aust.) Pty Ltd</b> .....	<b>1420</b>
<b>HARNISCHFEGER, Mr John Paul, Representative on behalf of South East Queensland Regional Organisation of Councils, Council of Capital City Lord Mayors, and Brisbane City Council</b> .....	<b>1326</b>
<b>JEREMY, Mr Richard Keith, General Manager, Australian Beef Association Ltd</b>	<b>1371</b>
<b>LOGAN, Mr Ian, National Competition Policy Project Manager, Brisbane City Council, Representative on behalf of South East Queensland Regional Organisation of Councils and Council of Capital City Lord Mayors</b> .....	<b>1326</b>
<b>MacDONALD, Mr Keith, Committee Member, Australian Coalition for Economic Justice</b> .....	<b>1432</b>

<b>McGOVERN, Dr Mark, Economic Adviser, Australian Beef Association, and Director, Rural Policy Institute . . . . .</b>	<b>1371</b>
<b>MILGATE, Ms Margaret Ann, Market Development Officer, Queensland Fruit and Vegetable Growers . . . . .</b>	<b>1399</b>
<b>MULLER, Dr Robert Louis, General Manager, Bundaberg Distilling Co. Pty Ltd</b>	<b>1420</b>
<b>O'HALLORAN, Mr Brian Francis, Committee Member, Australian Coalition for Economic Justice . . . . .</b>	<b>1432</b>
<b>ORANGE, Mr John William, Divisional Manager, Brisbane City Council, Representative on behalf of South East Queensland Regional Organisation of Councils and Council of Capital City Lord Mayors . . . . .</b>	<b>1326</b>
<b>PARLETT, Mr John James, Senior Manager, Tax and Industry Policy, Ernst and Young, on behalf of Bundaberg Distilling Co. Pty Ltd . . . . .</b>	<b>1420</b>
<b>SIMPSON, Mr Christopher James, Executive Officer, Banana Sectional Group Committee, Queensland Fruit and Vegetable Growers . . . . .</b>	<b>1399</b>
<b>WEATHERLEY, Mr Derek Ross, Research Assistant, National Credit Union Association Inc. . . . .</b>	<b>1360</b>
<b>WILSON, Mr Fred Albert, Director, National Credit Union Association Inc., and Manager, Queensland Police Credit Union Ltd . . . . .</b>	<b>1360</b>

**Committee met at 9.06 a.m.**

**CHAIR**—I call the committee to order. Today the committee continues its inquiry into the proposed changes to the Australian taxation system. The Senate referred the inquiry to the committee on 25 November 1998. This hearing continues the second stage of the inquiry. At this stage 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, the efficiency of the economy and future public revenues. The committee will report on the second stage of the inquiry by 19 April 1999.

This committee called for submissions to be lodged by 29 January 1999. In fact, the committee is still accepting submissions and so far has received well over 1,300. This is the first public hearing to be held by the committee in Brisbane in the course of this inquiry. In addition to this hearing, the committee will be conducting further public hearings around Australia. The committee has released the submissions relating to stage 1 of the inquiry and the submissions of those witnesses who gave evidence at earlier hearings. The committee does not intend to release all of the remaining submissions as yet, except for the submissions by the witnesses who are giving evidence today. Is it the wish of the committee that submissions 816, 464, 712, 459, 879, 596 and 1300 be made public? There being no objection, it is so ordered.

For the record, this is a public hearing and, 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 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.

[9.07 a.m.]

**HARNISCHFEGER, Mr John Paul, Representative on behalf of South East Queensland Regional Organisation of Councils, Council of Capital City Lord Mayors, and Brisbane City Council**

**LOGAN, Mr Ian, National Competition Policy Project Manager, Brisbane City Council, Representative on behalf of South East Queensland Regional Organisation of Councils and Council of Capital City Lord Mayors**

**ORANGE, Mr John William, Divisional Manager, Brisbane City Council, Representative on behalf of South East Queensland Regional Organisation of Councils and Council of Capital City Lord Mayors**

**CHAIR**—I welcome Mr John Orange of the South East Queensland Regional Organisation of Councils and other witnesses appearing with him. Mr Orange, do you have any comments to make about the capacity in which you appear?

**Mr Orange**—I am here on behalf of Councillor Jim Soorley, who unfortunately is unable to attend today.

**CHAIR**—I would invite you to make an opening statement.

**Mr Orange**—Thank you for the opportunity to appear before you today and to expand on our GST submissions. I would like to make three main points to enhance on the submissions that we provided you with but, before I do that, I would like to clarify a misunderstanding that arose from the hearings on 2 February in which Senator O'Chee talked about revenue savings through fuel reductions—fuel reduction savings—to Brisbane City Council in the order of \$13 million. He quoted the Queensland Local Government Association as the source of that information. We have been unable to determine with the Local Government Association of Queensland as to where that number came from. Our best estimate is that we will benefit by the tune of \$4.5 million, not \$13 million, but that when you add the impact of GST to the price of fares on transport, there will be a net cost to consumers of \$2.7 million. Thank you for the opportunity to clarify that.

The first point I would like to make to the hearing is that local governments currently suffer from an expanding role with a diminishing resource base. We are seeing more of the roles and responsibilities devolved from federal and state governments onto local government. At the same time, we are seeing increasing demand placed on us by our communities and our customers. While that has been occurring, the financial assistance that we have been receiving from the federal government has declined. From 1987-88, in real terms the decline for Brisbane City Council as an example has been 41 per cent. We would argue therefore that local governments should get access to a share of the GST and we are proposing a share of six per cent, which would take us back to that 1987-88 level.

We believe also that the share of GST should be passed to us through the federal government, not through the states as has been proposed. We believe that it is important that

local government be recognised by the federal government for its role and its responsibilities in delivering services to the community and we think it is important that the administration of revenues to local government continue to be done through the federal government.

The second point I would like to make is that the draft legislation as we currently see it is unclear as to what will be affected in local government in terms of the services provided, what will be affected by GST and what will not. We are told that rates and regulatory services will not, but we are not told exactly what commercial activities of local governments will. It is of concern to us. It makes it very difficult for us to calculate a model and we would argue very strongly that clarity needs to be provided in the legislation as to what exactly is covered and what is not. In that regard we think there may be some benefit in looking at the national competition policy definitions of what is commercial and what is not. We think that is probably a good start. If we look to reinvent another mechanism for defining commerciality, we will be duplicating processes and systems within local government.

The third point I would like to make is that we are really uncertain as to what the impact on demand will be and what the broader community impacts will be from applying GST to local government services. If you take Brisbane City Council as an example, we anticipate that transport patronage on our bus fleet will decline by some three per cent when GST is added to the prices, we anticipate that patronage of the arts and sports events in the venues that we run will decline by something between six and 11 per cent, and we are told by the rail associations that there will be a modal shift from rail transport for freight to road transport in the order of 10 per cent. When all these things are put together, local government is confronted with additional costs in maintaining infrastructure, and the communities that local governments represent are subject to the broader negative impacts of increased congestion, pollution, and accident costs that flow from increased usage of private sector vehicles at the expense of public sector. They are the three points that I would like to make, and I am prepared to take questions now.

**Senator MACKAY**—In relation to both the submissions that have been produced, the very issue that you described has been traversed in some detail, and that is the issue of where a GST is applicable, particularly in terms of where a nominal charge is applied, and quite often where you have effective cross-subsidy in relation to the rates base on what is regarded as really community service obligations from local government. I am interested in your suggestion that the NCP definition may be a useful one. Just for your information, we seem to now have clarification as to pretty much how this will apply via a number of mechanisms, particularly estimates a couple of weeks ago. It seems—and I am interested in your comments in relation to this—that a GST will be applicable in all areas of commercial activity, including where a nominal charge is applied.

This would seem—and I think this may have actually been raised at the hearings before—to have a major impact in relation to local government and suggestions from the government that we have received have included potentially increasing the rates in order to ensure that the councils are not substantially out of pocket or to ensure that the consumer is not out of pocket in terms of the CSO retention or, secondly, getting out of the field altogether in terms of services like swimming pools, child care, et cetera, that are affected. That seems to be the situation which is a bit of a different situation from what we

understood previously, so I am just interested to know whether you are aware of that and what the implications of that are.

**Mr Orange**—I was not, Senator. But I agree with you; it certainly changes the assumptions that we have made to date in doing our modelling. You are right. It will have an impact on the cost base for local governments and they will need to find ways to fund that shortfall. There is a direct impact, I guess, when you apply it to commercial activities, excluding CSOs, and that is the impact that has to be borne by the community. We have estimated in Brisbane's case that that impact will be in the order of \$16½ million. There are also the costs of administering and complying with NCP and also some one-off set-up costs associated with it, all of which ultimately will have to be borne by the community.

Add to that GST on CSOs and that number will increase significantly, I imagine. Again using Brisbane Transport as an example, we currently provide in the order of \$25 million worth of subsidies to Brisbane Transport. Apply a GST to that and we see a substantial change in the fares.

**Senator MACKAY**—Do you have any idea how local government will be able to cope with this?

**Mr Orange**—Local government will do a number of things. I guess it will continue to look at its own efficiencies, which it has done for a number of years now, but ultimately its hands are tied. It will have to react by either sourcing the revenue shortfall through rates or cross-subsidies, as you have looked at, or I think a worse alternative which is to look at, as you suggested, doing away with some of those services that are affected, and that has a negative impact on employment and the communities that we are trying to serve.

**Senator MACKAY**—In relation to the abolition of FAGs and the ceding of powers to the states, in both submissions you also have traversed that in some detail. What is your information about what sort of mechanism would apply in relation to ensuring that the states did not, I think as you have said, cannibalise the local government money?

**Mr Orange**—I am not aware that guidelines had been put in place for the states to abide by and that concerns us. We are in discussion with the state government here on behalf of the South East Queensland Regional Organisation of Councils and, more broadly, the whole of Queensland local government. We are talking to the state about, if we do not get our recommendation adopted, what mechanisms we can adopt to put that in place. I understand that it will be a state by state arrangement and that concerns us, because what it will do is take away local government's capacity to organise itself nationally and lobby nationally for a fair and equitable share. It would be up to each state and each local government body within that state to negotiate.

**Senator MACKAY**—Have you done any work in relation to the modelling of (a) the impact of a GST along with the revelation I indicated to you earlier and (b) the compliance costs?

**Mr Orange**—We have done some on compliance costs. We will have to take that information away and remodel our models to see the impact of GST on CSOs. We base our

compliance costs on research that was done on the New Zealand model, which estimated that seven per cent of the GST take would be absorbed in administrative GST. For Brisbane City Council as an example, that comes to \$1.2 million. Add to that other costs that Brisbane City Council will have to absorb: for example, in our fleet management we have seen a significant reduction in the value of our assets already occurring because wholesale sales tax coming off vehicles will reduce the price of those vehicles and therefore the resale value of that fleet which exists at the moment is significantly declined. We will have negative cash flow impacts in terms of Brisbane City Council in administering the GST and we will have one-off set-up costs in the order of \$1½ million, we estimate, to deal with systems changes.

When you think about how it will impact local government, it will go right from the major accounting systems infrastructure that we have through to every receipting instrument that we have in all of our customer service centres around Brisbane. So it is a not an insignificant amount of work that has to be done in terms of systems, in terms of mind-set and people change and in terms of ongoing administration.

**Senator MACKAY**—One final question, Chair: a number of rural and regional councils, particularly in Queensland, actually rely on FAGs particularly to provide the substantial proportion of their revenue base. In some councils I think that is up to 60 to 70 per cent. Have you done any work on how the abolition of FAGs will impact on those rural and regional councils?

**Mr Orange**—We have not with this submission. I understand that the Local Government Association of Queensland may well have done that sort of work. Clearly, though, we can draw a conclusion that it will undermine their ability to provide services to the community in a not dissimilar way to the way that it will affect, say, Brisbane City Council, the difference being though that they have a greater reliance on it, as you point out. We have not done modelling on that basis.

**Senator O'CHEE**—Mr Orange, do you believe the Brisbane City Council is operating as leanly and as efficiently as it possibly could?

**Mr Orange**—Senator, we have undertaken reform in Brisbane City Council in advance of national competition policy reforms being forced upon us, if you like, through legislative change. So we have been proactive and front-footed. We have been reforming for five years now, so I would say that we are a considerably different organisation today than we were five years ago and a major part of that difference has to do with significantly increased customer service, greater efficiency in the way that we deliver our services to the ratepayers and the customers of Brisbane City Council, and a lower and leaner approach to managing our operations.

**Senator O'CHEE**—So I assume the answer to that is yes.

**Mr Orange**—Yes.

**Senator O'CHEE**—How much was spent the other day on hosting Gerry Adams?

**Mr Orange**—I do not have the answer to that.

**Senator O'CHEE**—I thought if it was a lean, efficient operation you would know that answer.

**Mr Orange**—No, I do not have the answer to that. I do not have the number with me.

**Senator O'CHEE**—The council runs a fleet of ferries, doesn't it?

**Mr Orange**—It does.

**Senator O'CHEE**—What is the total cost of operating that fleet of ferries?

**Mr Orange**—I do not have the answer to that. I can take that on notice and get back to you.

**Senator O'CHEE**—What is the total cost of operating your bus fleet?

**Mr Orange**—The total cost of operating the bus fleet is in the order of \$90 million.

**Senator O'CHEE**—Ninety million? How do you work that out?

**Mr Orange**—I am recalling information that I have seen, Senator. Do you mean how is that number constructed?

**Senator O'CHEE**—Yes.

**Mr Orange**—That is operating costs based on costs of operation, so it is the buses that we operate, depreciation associated with those buses, provision of services and maintenance associated with those buses. It incorporates labour costs, wages and salaries—the normal sort of operating costs, Senator.

**Senator O'CHEE**—How much of that is fuel?

**Mr Orange**—I have that number, Senator. We use almost 15 million litres of fuel a year for Brisbane Transport.

**Senator O'CHEE**—How much fuel do you use generally?

**Mr Orange**—The only additional fuel is about 2.85 million litres for our other general plant and vehicles.

**Senator O'CHEE**—What is your total bus revenue?

**Mr Orange**—Sixty-four million dollars.

**Senator O'CHEE**—And that represents how many passenger trips?

**Mr Orange**—Fifty million.

**Senator O'CHEE**—What is your revenue on ferries, for example?

**Mr Orange**—We do not have that, Senator.

**Senator O'CHEE**—You would not know how many people travel on them?

**Mr Orange**—We do, but I do not have the information. I can provide you with that.

**Senator O'CHEE**—Yes. It just makes it a little bit difficult to work out exactly how leanly and efficiently you are working if you cannot give us the figures. You say you have costed all this out.

**Mr Orange**—We have, Senator. Senator, I was not aware that you were going to go into detail in examining the cost base of the Brisbane City Council. Had I known that, I would have brought more information with me.

**Senator O'CHEE**—Mr Orange, my simple question is based on the premise that you make representations to us and we should test out those representations. You see, otherwise, it is a pretty meaningless exercise.

**Mr Orange**—But, Senator, the representations I have made are not about Brisbane's cost base.

**Senator O'CHEE**—You are saying these things are going to impact on the operating costs of councils. I just want to put you to the test.

**Mr Orange**—They are, yes, and I have provided you with information.

**Senator O'CHEE**—I am not willing to have an argument, Mr Orange. What I am saying to you is it is difficult to put you to the test if I cannot get the details from you.

**Mr Orange**—Senator, I am happy to provide you with the calculations. For example, shall we take the fuel issue: 15 million litres of fuel, savings per litre 25c, annual savings for the bus fleet \$3.7 million, add to that the other transport costs where we have savings of about \$800,000 and that comes to the total of \$4.5 million I talked about earlier on, and that is considerably—

**Senator O'CHEE**—Because the LGA—

**Senator CONROY**—Thirteen—

**Mr Orange**—Correct, obviously.

**Senator O'CHEE**—Well, congratulations!

**Senator FERGUSON**—It has taken Senator Conroy 10 minutes—

**CHAIR**—Order! Senator O'Chee.

**Senator CONROY**—He is very concerned about the number of buses on the road when he walks backwards from the Gold Coast, so—

**CHAIR**—Order! Senator O’Chee.

**Senator O’CHEE**—Thank you, Mr Chairman. You will have to forgive Senator Conroy. He gets a little excited in the mornings. Okay, so let us leave that to one side. You cannot give us the figures on that. The LGAQ, though, provided a series of cost savings based on figures provided by the council to the LGAQ in September 1998. Have you contacted the LGAQ?

**Mr Orange**—We have.

**Senator O’CHEE**—Because it was the subject of some correspondence between my office and the LGAQ.

**Mr Orange**—Provided by the Brisbane City Council.

**Senator O’CHEE**—To the LGAQ.

**Mr Orange**—We have spoken to the LGAQ and asked for the source of that information. They are not aware of where that information came from, and we are certainly not aware of where the numbers came from to support that.

**Senator O’CHEE**—Yes. Well, that was what they said to me, and they said they had obtained that from you.

**Mr Orange**—We have spoken to them and they have said that that is not the case.

**Senator O’CHEE**—Okay.

**Mr Orange**—We will just have to leave that on—

**Senator O’CHEE**—Let us go through this business about commercial operations. You believe that the commercial operations of council should or should not be subject to GST?

**Mr Orange**—We believe that the commercial operations of council are caught under the current definition of what is GSTable. What we are not sure about, though, is the extent to which commercial operations would be caught; that is, the definition is not clear.

**Senator O’CHEE**—Okay, but do you believe they should or should not be subject to GST?

**Mr Orange**—I guess if we had our preference we would say they should not, but we are recognising the reality.

**Senator O'CHEE**—But if you had your preference and they were not, then a council commercial operation competing with a private sector commercial operation would get a tax advantage, and that would not be very fair, would it?

**Mr Orange**—Senator, there is a mechanism at the moment that we operate under national competition policy which creates a level playing field environment, which is the tax equivalence regime.

**Senator O'CHEE**—But it would not be fair for you to not have to pay taxes or charge taxes that private sector competitors did, would it? It wouldn't.

**Mr Orange**—The fairness would be in the way that we compete with the private sector. The fairness would be whether we calculate our prices incorporating an adjustment for GST so that we do not take private sector business opportunities away from them in an unfair way.

**Senator O'CHEE**—But you would get a profit—

**Senator FERGUSON**—You would get a bigger profit than the private sector.

**Mr Orange**—That is correct, and that is what the tax equivalence regime is about.

**Senator O'CHEE**—But do you think making a bigger profit than the private sector competitor is fair?

**Mr Orange**—What I am saying is that there is a mechanism; it is the tax equivalence regime. That could take account of notional GST payments which would ensure that prices provided by local government commercial operations would not be undercut by the fact that GST is not applied. Therefore the competition would be on a level playing field.

**Senator O'CHEE**—Do you think the businessmen in competition with you would find it fair that you would get a bigger profit, charging the same price, because you have a tax break that he or she does not have?

**Mr Orange**—Senator, there would not be a bigger profit. There would not be a bigger profit.

**Senator FERGUSON**—Why not?

**Senator O'CHEE**—Why not? You are charging a higher price.

**Mr Orange**—But we are not charging a higher price; we are charging an equivalent price.

**Senator FERGUSON**—Can I give you an example—

**CHAIR**—Order! Can we have one at a time and let the witness answer, please.

**Senator FERGUSON**—Senator O’Chee, can I just continue along that same line. In a small country council or shire or whatever you might call them here, if the council runs a caravan park and does not pay GST and a private operator alongside has a privately owned caravan park and is subject to GST, are you telling me that the council would put its prices up to the level of the private operator so in fact there would be no unfair advantage, and that the council would not pocket the profits?

**Mr Orange**—I am saying there is a mechanism that would enable that to happen, which is the tax equivalence regime.

**Senator O’CHEE**—So what happens to the additional profit that you make?

**Mr Orange**—Can you explain ‘the additional profit’, Senator?

**Senator O’CHEE**—You said you would calculate your prices so that they were the same as a business paying tax, but you are not paying the tax.

**Mr Orange**—That is correct.

**Senator O’CHEE**—So there is an additional profit.

**Mr Orange**—I see where you are coming from. Yes.

**Senator O’CHEE**—There is, isn’t there? So how happy do you think one of your rate-paying small businesses would be if you had your way and you just took an additional profit because you got a tax break that they didn’t get? Do you think they would find that fair?

**Mr Orange**—The commercial business of the council are you asking about?

**Senator O’CHEE**—No, I am asking about the small business competitor.

**Mr Orange**—The competitive commercial business?

**Senator O’CHEE**—Yes.

**Mr Orange**—The competitive commercial business is operating to make a profit and it competes on price with, in some instances, local government businesses. If those prices are set on a level playing field basis then the private sector operator is entitled to make a profit in the same way that a local government operator is.

**Senator O’CHEE**—Mr Orange, I will ask you the question again. If you were a small business operator in competition with a council that did not bear the tax and took an additional profit whilst charging the same price, do you think that would be fair in terms of the levels of profits the council received?

**Mr Orange**—To the small business competitor?

**Senator O'CHEE**—To the small business competitor. Do you think they would find that fair that you get an additional profit they do not get?

**Mr Orange**—I think they would be concerned that they were potentially losing business, but if the prices were equivalent then they have an equal opportunity.

**Senator O'CHEE**—We might see what some of the ratepayers say about that. Let us move on.

**Mr Orange**—The ratepayers, Senator—

**Senator O'CHEE**—You have accepted the fact, Mr Orange, that the government has decided, for reasons of fairness, that when you have a commercial activity it should be subject to GST.

**Mr Orange**—We have accepted that it is likely that GST will apply to commercial activities.

**Senator O'CHEE**—So why shouldn't we make sure that every one of those commercial activities is caught? Why should we allow you to slip some through the net?

**Mr Orange**—But, Senator, we are not asking for ones to be slipped through the net. We are actually asking for clarity. That is what is in the submission. We want clarity as to what is caught and what is not caught. What we have at the moment is uncertainty, and it is very difficult for us to determine how we are going to implement the reforms within our organisations.

**Senator FERGUSON**—But you do not know what your commercial activities are, though.

**Mr Orange**—We do.

**Senator O'CHEE**—If you know what your commercial activities are, you should not have much of a problem.

**Senator FERGUSON**—You should not have much of a problem.

**Mr Orange**—So it has been defined as 'all commercial activities'?

**Senator O'CHEE**—You know that a commercial activity is a commercial activity. You say you know what they are. Then you should not have any great drama about it, then, should you?

**Mr Orange**—But, Senator, what about something like parking meters? That is run as a commercial operation within Brisbane City Council. That means that we should be applying GST to every parking meter in the city, in your definition?

**Senator O'CHEE**—Yes.

**Mr Orange**—Okay. Well, that will incur some significant costs and some very interesting calculations to the charges put on the parking meters. What about waste services where we are encouraging recycling? We charge tip fees

**Senator O'CHEE**—Just going back to parking meters, Mr Orange, you are charging people to park on the street. The alternative is they park in a private car park.

**Mr Orange**—Some of which we own, yes.

**Senator O'CHEE**—Some of which you own, yes, but there are some that you do not own.

**Mr Orange**—That is correct.

**Senator O'CHEE**—Why should you have a situation where you do not have to charge or collect GST on your parking operations when a private sector person does?

**Mr Orange**—I was arguing, Senator, more about the difficulty in applying it to individual parking meters and the costs associated with that. We acknowledge that in our parking stations GST would apply equally with those of others.

**Senator O'CHEE**—But every time Councillor Soorley raises the cost of parking in the street by jacking up the charge on meters, he does not run off to the federal government to say, 'Look, we're going to increase the fees on the parking meters. We'd like you to give us a handout to do it so we can make some more money.' He has never complained about this in the past where he has jacked up the price of parking on the street, has he?

**Mr Orange**—No, I do not believe so.

**Senator O'CHEE**—No, he absorbed the cost every time.

**Mr Orange**—We absorbed the cost of what, Senator?

**Senator O'CHEE**—Of recalibrating meters every time you have put up parking fees. You never complained about it then.

**CHAIR**—In those other cases that Senator O'Chee may have been referring to where you have absorbed the cost, were they cases where the federal government had imposed a new tax on you?

**Mr Orange**—Sorry, Senator, I am unclear as to your question.

**CHAIR**—Senator O'Chee was saying that on previous occasions you have absorbed the cost of recalibrating your parking meters when the council in its wisdom decided to increase charges. All I was asking was: were those occasions where the federal government had decided to impose a new tax on you?

**Mr Orange**—No, they were not.

**Senator BARTLETT**—I have just a few questions around the issue of what you said earlier on about looking for a guaranteed six per cent component of the GST and wanting that coming from the federal level. Firstly, just with some of the potential negative impacts that you have outlined today, if you were able to get that guaranteed six per cent of the GST as a growth tax, do you think that that would over time overcome some of the more immediate negative impacts you have outlined?

**Mr Orange**—Senator, I think it would certainly go a long way to helping us. It would help us meet the costs of implementation and the costs of compliance and administration associated with it. It would enable local governments to position their businesses and their operations in such a way as to meet the community needs. One of the problems that we are faced with, with GST, is the change in demand. We just do not know what is going to happen in terms of demand. We have done some modelling and we speculate that it will have some impact on our services. To the extent which demand falls—for example, in transport operations—a local government like Brisbane City Council will be left with a greater shortfall in revenue in its operations and that will have to be funded, so the sorts of suggestions that we are making about the six per cent would, I agree, offset those sorts of things.

**Senator BARTLETT**—If you were able to get that guarantee of six per cent, why is it so fundamental that that six per cent guaranteed chunk of money comes direct from federal government rather than through the state?

**Mr Orange**—Senator, we are concerned that, if the responsibility is devolved to the states, it will mean that there will be a series of individual negotiations that will be subject to, as we understand it, no defined rules or procedures as yet. It means the outcomes could be different and we are concerned that there could be different outcomes for the same state over different political regimes, for example. We are also concerned that it, in a way, reduces the recognition of local government as a legitimate level of government within Australia because it further implies that local government is tied and linked to the states.

**Senator BARTLETT**—You are not specifically saying you do not trust state governments or you trust federal government more than you trust state government?

**Mr Orange**—We think there would be greater uniformity and consistency coming from federal government.

**Senator BARTLETT**—So, if they shafted one state, they would shaft them all equally.

**Mr Orange**—They are your words, Senator. Yes.

**Senator BARTLETT**—But there is no particular greater benefit from a federal rather than a state level, other than some of those, if you like, symbolic things about the importance of local government in its own right?

**Mr Orange**—And the consistency. The consistency argument is important from the local government perspective. The peak body, the Council of Capital City Lord Mayors, would be concerned that the arrangements put in place in one state may not be similar to arrangements

put in place in another state. In fact, we have seen that in the way that various state governments have applied some of the benefits of the national competition policy. In Queensland we have benefited from having very good relationships with our state government and we have benefited by sharing in some of those implementation costs through passing through the federal moneys from the state government. That has not been the case in other states and that is an example of the sort of disparity that could occur if we did not have a consistent federal approach to it.

**Senator BARTLETT**—Are many of the councils in the south-east Queensland region involved in housing services at all?

**Mr Orange**—Yes, to a lesser extent than the state government clearly, but there are roles in housing. Brisbane City Council does have some roles in housing.

**Senator BARTLETT**—Has there been much analysis of the impact on the housing roles?

**Mr Orange**—We have not done a great deal of impact on housing analysis.

**Senator BARTLETT**—Is some of that area in terms of Brisbane City Council in relation to boarding houses and low cost accommodation in the inner city area?

**Mr Orange**—Yes. We work with the state in providing the regulatory framework for those sorts of things and also in encouraging development where it is appropriate in those areas.

**Senator BARTLETT**—So not so much direct service provision?

**Mr Orange**—Not so much direct service provisions.

**Senator HARRADINE**—You represent all the capital city mayors, do you?

**Mr Orange**—That is correct, Senator.

**Senator HARRADINE**—And you are all as one that the allocations should be applied on an equal basis. What basis is that?

**Mr Orange**—Senator, that is the six per cent share of GST.

**Senator HARRADINE**—Yes, I know that, but on what basis is that then distributed?

**Mr Orange**—We would like to talk to the federal government in terms of establishing a mechanism.

**Senator HARRADINE**—No, you are talking to us. What basis? It is an equal basis for that distribution. Is it a per capita basis or what?

**Mr Orange**—Senator, we would argue for a per capita basis, but—

**Senator HARRADINE**—Is that agreed to by all of the mayors of the capital cities?

**Mr Orange**—That was what I was going to say, Senator. We have not established that agreement at that level.

**Senator HARRADINE**—You come before us and suggest that you all want to be dealt with equally or shafted equally, so it is not a policy. What you are saying to us is not the policy of the capital city mayors.

**Mr Orange**—Senator, what the argument is from the capital city lord mayors is that we establish a mechanism for sharing that on a fair and equitable basis.

**Senator HARRADINE**—Which is what?

**Mr Orange**—Well, Senator, we have not worked that mechanism out.

**Senator FERGUSON**—Mr Orange, your submission has been sent in by Councillor Soorley on behalf of the capital city lord mayors, I take it. Who prepared the submission?

**Mr Orange**—We did, Senator.

**Senator FERGUSON**—Who is ‘we’? A committee or a group of—

**Mr Orange**—A group of people at Brisbane City Council, in consultation with the capital city lord mayors—the capital cities.

**Senator FERGUSON**—So it was actually prepared by the City of Brisbane Council but in consultation with all of the other people. That might explain why the submission is to the Senate committee inquiring into the GST and the new tax system when in fact we are only inquiring into a new tax system of which GST is a part, and even the title of the committee is wrong.

Throughout the whole of this submission it does not refer to a new tax system really; it only refers to the GST and the impact of a GST. Does that mean that the Council of Capital City Lord Mayors has no comment to make on all of the other aspects of the new tax system?

**Mr Orange**—Senator, it does refer to new aspects of the new tax system, specifically to components that are being referred to—reciprocal taxation and a national tax equivalence regime—and we make strong recommendations in that submission on both of those.

**Senator FERGUSON**—But nowhere in the submission does it talk about the income tax cuts that will be available to all the people in Queensland which will enhance their capacity to pay and offset the effects of the introduction of a GST. That is not taken into account anywhere?

**Mr Orange**—It does not refer to that, Senator.

**Senator FERGUSON**—Yes. Because I am quite sure that Queenslanders who will receive those tax cuts would think that is an integral part of the new tax system. I also ask you: can your figures of a 10 per cent shift from rail to road be substantiated, or did they come from the Australian rails commission?

**Mr Orange**—The railway association of Australia is the source of that information.

**Senator FERGUSON**—Yes. I think they appeared before us and I am not sure that they had any substantive figures either. It was an estimation rather than based on substantial research. How much will your council save in FIDs and BADs?

**Mr Orange**—Sorry?

**Senator FERGUSON**—The bank taxes. The financial institutions duty?

**Mr Orange**—They do not apply in Queensland.

**Senator FERGUSON**—And BADs? None at all in Queensland?

**Mr Orange**—No.

**Senator FERGUSON**—Okay. They do in every other state. I can tell you that.

**Mr Orange**—Yes.

**Senator FERGUSON**—In relation to your bus fleet where you gave some answers to Senator O'Chee, I think you said the cost of running the bus fleet was some \$64 million, if I remember rightly.

**Mr Orange**—That is the revenue.

**Senator FERGUSON**—That is the revenue?

**Mr Orange**—Yes.

**Senator FERGUSON**—Okay, the revenue from the bus fleet is \$64 million and I am not sure, but you have also said that your savings in fuel tax will be in the order of \$4.5 million—this is your figures—and I think you said \$3.6 million will be saved in the fuel costs of running that bus fleet.

**Mr Orange**—Yes, \$3.7 million.

**Senator FERGUSON**—Just on a rough calculation, if your revenue from running the buses is that and your savings are \$3.7 million, which I have roughly calculated to be close to six per cent of its running costs, why on earth would you put your fares up by 10 per cent?

**Mr Orange**—The fare increase is \$6.4 million. That is the application of GST on the fares. It will be \$6.4 million. The net increase that will go on fares is \$2.7 million.

**Senator FERGUSON**—How do you get that figure of \$6.4 million as an increase in fares?

**Mr Orange**—That is the application of the GST on them.

**Senator FERGUSON**—Yes, but hang on, you have just dropped your running costs by \$3.6 million just in the diesel that you run your buses on. So what are you going to do—pocket that \$3.6 million?

**Mr Orange**—No, because we are talking about a net increase of fares. That \$2.7 million is a net increase in fares, which is an average of 6c per trip.

**Senator FERGUSON**—Six cents per trip?

**Mr Orange**—Yes.

**Senator FERGUSON**—So your fares are not going to go up by 10 per cent, are they?

**Mr Orange**—No, but we have calculated it to get a net.

**Senator FERGUSON**—That's right, so you have not actually taken into account the \$3.6 million?

**Mr Orange**—We have taken that into account.

**Senator FERGUSON**—To get a net increase?

**Mr Orange**—Yes. Yes, the net increase is \$2.7 million.

**Senator FERGUSON**—Where does your \$6.4 million come from?

**Mr Orange**—We have done it on a gross basis. We have taken the gross amount of the savings from fuel, we have taken the gross effect of the GST, and we have taken one off the other and that gives a net increase.

**Senator FERGUSON**—So in actual fact what will happen in Brisbane is that fares are likely to go up, at the most, by five per cent.

**Mr Orange**—That is correct, Senator. That is the number we came up with, five per cent.

**Senator FERGUSON**—I think it is pretty clear when you talk in your submission about adding a GST caused increase of 10 per cent to public transport fares—that is what you say in your submission—that that is not a correct statement, is it?

**Mr Orange**—That is not a net statement, Senator.

**Senator FERGUSON**—It is not a correct statement.

**Mr Orange**—It is talking about the gross effect of GST.

**Senator FERGUSON**—It is not a correct statement because you have just said that fares would only go up by five per cent.

**Mr Orange**—Senator, it is correct if it is interpreted as being gross.

**Senator FERGUSON**—You are using a lot of fancy interpretations because when you want to use gross to add on 10 per cent, you are adding on 10 per cent, but you say that your final net figure is going to be five per cent.

**Mr Orange**—That is correct.

**Senator FERGUSON**—I think that the fare-paying public would be much more concerned to know that fares under a 10 per cent GST are only going to go up by five per cent than your submission which says that there will be a GST caused increase of 10 per cent to public transport fares. It is there in black and white. You then say it has the potential to divert three per cent of the existing users away from Brisbane Transport. How did you arrive at the three per cent figure?

**Mr Orange**—That is based on transport modelling and the elasticity of demand. We anticipate that patronage will decline by three per cent based on the net five per cent increase.

**Senator FERGUSON**—Could you supply us with details of that modelling, because we have done a lot of work with modellers in recent times and their assumptions have been questioned in lots of cases, including Treasury's.

**Mr Orange**—Yes, Senator, we can supply that.

**Senator FERGUSON**—I would like to see that modelling, because, if you are basing that three per cent shift on modelling, I think we should know that those figures can be substantiated.

**Mr Orange**—Yes.

**Senator FERGUSON**—Thank you.

**Senator MACKAY**—Are you aware of any modelling that has been done by the federal government into the impact of the new tax system on local government?

**Mr Orange**—No, Senator. We are aware of the outcomes of some assessments that have been done. For example, we were aware that there is an estimate of \$70 million worth of benefit being available to local governments, but we do not know how that number is made

up and therefore we cannot work out what proportion of that number will apply at an individual local government level.

**Senator MACKAY**—As far as we are aware there has not been, but if there is perhaps we could be provided with it, Chair. Just away from buses and ferries and things, what services does local government provide, broadly?

**Mr Orange**—The things that will be caught by GST? We can give you a list of those, Senator.

**Senator MACKAY**—That would include things like libraries, seniors centres, swimming pools.

**Mr Orange**—Exactly—car parking, refuse tips.

**Senator MACKAY**—School holiday programs?

**Mr Orange**—Yes.

**Senator MACKAY**—Let us get it very clear again: do you think that the GST ought to apply to areas of commercial activity such as pools, seniors centres, school holiday programs, et cetera, where a nominal fee is charged?

**Mr Orange**—Senator, we do not think that they should apply to those areas where we see there is a community service being provided.

**Senator MACKAY**—I'm sorry, I interrupted you. Would you mind just reading that list out.

**Mr Orange**—Yes, sure: car parking fees, refuse tips and hazardous waste fees, commercial sales of items that we provide, search and ownership transfer fees, facility hire, administration fees, green fees, building application fees, cemeteries and crematoria. What we were not aware of when we did this list was that it would apply to those community services that you have spoken about. So you can add to that list library services and pools. We do some work, for example, in immunisation and we do work with mosquito and pest control and a large number of things.

**Senator MACKAY**—Why weren't you aware that GST would be applicable to commercial activities where a nominal fee was charged?

**Mr Orange**—Because it was not clear, Senator, in the information that we were able to obtain.

**Senator MACKAY**—Are you aware that there was a letter produced during the election campaign sent to local government in New South Wales by the National Director of the Liberal Party, Lynton Crosby, who said very clearly in the correspondence that GST would not be applicable to commercial activities where a nominal fee is charged?

**Mr Orange**—I was not aware of that.

**Senator MACKAY**—That letter exists. Are you also aware that we have actually asked the government about this election commitment and the relevant minister has indicated that Lynton Crosby, the Director of the Liberal Party, was wrong when he made that assertion?

**Mr Orange**—I was not aware of that.

**Senator MACKAY**—What I am saying is, I do not blame you for being confused in relation to it. Can I just come back to the issue that you raised on all these services that are provided by local government, and the community service obligation. In relation to the plethora of services provided, you say a nominal fee is charged. What would be the general cross-subsidy, for want of a better term, from the rates base?

**Mr Orange**—Senator, on those services—libraries, for example—there is only a minimal recovery of fee for service.

**Senator MACKAY**—So it is not full cost recovery is what you are saying.

**Mr Orange**—It is not on those areas at all.

**Senator MACKAY**—What proportion of full cost recovery would it be?

**Mr Orange**—The cost recovery?

**Senator MACKAY**—If you were to go from nominal current regime to full cost recovery, what would be the average increase?

**Mr Orange**—In price?

**Senator MACKAY**—Yes—in percentage terms?

**Mr Orange**—I think a 90 per cent adjustment.

**Senator MACKAY**—So you are saying that the cross-subsidy from the rates base to the services like swimming pools, libraries, et cetera, is worth about 90 per cent?

**Mr Orange**—That would be right, in those sorts of things, yes.

**Senator MACKAY**—How many people in the private sector, do you think, would be prepared to subsidise these sorts of services by 90 per cent?

**Mr Orange**—Not many, Senator.

**Senator MACKAY**—I think that is the point, isn't it?

**CHAIR**—I think Senator O'Chee has a question for notice.

**Senator O'CHEE**—Yes, Mr Chairman. Mr Orange said that Brisbane City Council applies an equivalency regime to its costing, its services. That means, I assume, that under the equivalency regime they incorporate a notional cost for wholesale sales tax on the operating costs of its bus fleet and other vehicles. I was wondering if Mr Orange could take on notice, along with the other figures about ferries and so on, the notional saving as a result of the abolition of wholesale sales tax under the equivalency regime.

**CHAIR**—I think you are nodding in the affirmative, Mr Orange.

**Mr Orange**—I will take it on notice.

**CHAIR**—I have a couple of questions. We had His Honour the Mayor of Kalgoorlie before us last Wednesday in the fair city of Kalgoorlie. He said that charges on his council, on his city, were such that he would have to reduce services to his ratepayers. Given the higher costs, the only way out was to increase rates, sack people or decrease services, or go into deficit and that, while it was a matter for council, the only way in which he could see he could handle that would be to reduce services. There is an iron logic about budgets; they do not give and they are not negotiable; the figures speak one way or the other. Do I understand from your evidence this morning, just cutting to the chase, that what you are saying is you will be passing on some costs but in other areas reducing services?

**Mr Orange**—Senator, that is the outcome. That is the reality that we are faced with.

**CHAIR**—I was interested to hear the deputy chair of this committee, Senator Ferguson, say that of course there are tax cuts. I have never heard the government, I might say, tell people that the tax cuts are earmarked to be handed back to local government and to other providers of goods and services because of the higher charges they will have to make. I have never heard that said, but this morning Senator Ferguson did say, 'Well, that's one of the reasons for the tax cuts.' As an aside, I just wonder what, therefore, the net value of the tax cuts is, rather than the gross value, which seemed to be an argument that you were having with Senator Ferguson earlier about the meaning of net and gross.

Where you are passing on costs, would the council show what the real cost is, plus the cost to the council of a GST, on the ticket or on the charge that it was passing on, so that consumers could identify what was a legitimate council charge and what was the federal government cost of the GST?

**Mr Orange**—Yes, Senator, that is the intention. When we are looking at implementing GST, that will be one of the components of implementing it, as to how we split out those components—in receipting, in billing.

**CHAIR**—You would do this in the interests of transparency so that people could understand what were taxes and what were legitimate costs to the council?

**Mr Orange**—Yes, Senator.

**CHAIR**—You are aware that the government has said that it will not legislate for the GST cost component to be shown on price labels?

**Mr Orange**—Yes, I am aware of that.

**CHAIR**—Would you be doing this as a duty to your ratepayers, or consumers, so that they know what in fact the cost really is?

**Mr Orange**—It is a transparency issue, Senator.

**CHAIR**—Thank you. I have no further questions. Thank you very much for your attendance this morning and for the assistance you have given the committee in its inquiry.

**Mr Orange**—Thanks, Senator.

[10.02 a.m.]

**BRICKNELL, Mr Raymond Leo, National President, Australian Investors Association**

**FUNNELL, Mr Geoffrey Robert, Vice-President, Australian Investors Association**

**CHAIR**—Mr Bricknell, do I acknowledge you first and do you, on behalf of the organisation, propose to present an overview of your submission and take questions, along with your colleague?

**Mr Bricknell**—Mr Chairman, with your permission, basically I will do the presentation to your committee. We were told that we had 45 minutes. I am planning, if that is okay, to use 20 minutes of that to lay our case in front of you and that leaves the other 25 minutes for questions. Is that acceptable?

**CHAIR**—I think the committee would probably prefer a shorter period of presentation, but please proceed and see what we can manage.

**Mr Bricknell**—All right. Perhaps you will stop me when—

**CHAIR**—I do not want to stop you in putting your views before us, but if I read the mood of this committee, it is that they do prefer, having read your submission, to ask questions. But please proceed, if you would not mind. I am not wanting to ruin your flow, if you have prepared a brief, but please bear in mind that in this case probably the more succinct the better.

**Mr Bricknell**—Okay. The Australian Investors Association supports the notion of wholesale reform of the Australian taxation system in the present political environment, provided that the reform covers the complete range of taxes, including business taxes, is comprehensive and is equitable to all. We wish to stress that we are not a nimby organisation, in that we are not here simply to argue for a better deal for our members at the expense of others. We are conscious of the fact that in any revenue neutral reform of the tax system, for every winner there must be a loser. We are concerned that many of the losers from the introduction of a GST will not be identified until after the event and therefore will go uncompensated.

If it is necessary to pay compensation to groups disadvantaged by changes to the tax system. Such compensation, we believe, should be in such a form or forms that cannot be whittled away by future inflation or by legislative or regulatory changes in the future. Indeed, if necessary, such compensation should be by cash up front as part of the true cost of tax reform. We are concerned that the history of compensation in other countries is that it was quickly dissipated. The AIA submits that it is more important that the current Senate inquiries be thorough, comprehensive and complete, rather than be constrained to meet any politically imposed deadlines for completion of the process.

Our members are largely self-funded retirees or people approaching that stage in their lives. Typically they have never drawn a cent in social welfare of any kind in their lives and, indeed, most have created jobs for others during their working lives, often in small

businesses, and simultaneously have raised their children to have a strong work ethic and to be self-reliant. Research shows that such children are most unlikely to ever join the ranks of the unemployed. In light of all the above, we respectfully request that the Senate treat individual investors fairly and sympathetically in the process of tax reform, not as a wealthy group whose interests can be ignored 'because they can look after themselves'.

Specifically, we ask the Senate inquiries to take account of the following couple of propositions when conducting their reviews of the GST and tax reform generally. Firstly, any shift in the system of collecting taxation from income to expenditure impacts on our members effectively as retrospective legislation. Having paid substantial income taxes at the prescribed rates whilst accumulating their savings, any sudden swing from income to expenditure taxation effectively taxes those with savings a second time. Indeed, the savings and standard of living of self-funded retirees are effectively reduced by whatever net percentage increase in the costs of their purchases occurs as a result of the introduction of a GST type tax after or close to their retirement. Most of the goods and services consumed by people in their latter years are not currently taxed under the wholesale sales tax system.

Secondly, any compensation offered to those with savings for a net reduction in their purchasing power should be provided in the form of up-front cash so that such compensation cannot be clawed back or whittled away, and should not cut out below, say, \$1 million in savings. The \$1,000 to \$3,000 amounts of means tested compensation proposed in the government's new tax system are so trifling as to be laughable, if indeed the matter were not so serious.

We ask you to consider this scenario: a person has savings of \$500,000 which cannot reasonably be replaced through working due to their age, and hence capital preservation is their overriding consideration in investing. A conservative balanced portfolio of investments is earning them, say, six per cent per annum, which is about the maximum they can achieve with reasonable capital security at this time. This gives them a taxable income of \$30,000 per annum, with their income tax reduced by any imputation credits received. At this level of income, they receive no government pension or associated benefits, pay full price for everything they buy, and can enjoy only a very modest standard of living. Replacement of items of a capital nature when they wear out—for example, cars, video recorders and the like—is a real challenge for such people. We are conscious of the fact that the minimum wage is about \$20,000 a year, and that is considered in many cases to create a class of working poor, so \$30,000 a year is not a high income.

If you now add a GST type tax such that many or most of the now largely untaxed items that these retirees buy—such things as food, movie tickets, car and house repairs, travel, quite a long list—increase in price by an average of, say, seven per cent as a result of a GST, then surely it is reasonable to compensate such people with an up-front cash payment of seven per cent of the total value of their investment portfolio, at least up to a portfolio value of, say, \$1 million. Remember that the apparently wealthy person with \$1 million in savings has an income of \$60,000 a year and, given that that person had to come from a high income background to be able to save \$1 million, \$60,000 is not a huge income for a couple.

Why should such people have their entire standard of living that they have worked and saved for all their lives reduced simply because a GST is introduced after they retire, or just before they retire? What have they done to deserve retrospective retribution? Such fair and adequate compensation should form part of the total recognised cost of any wholesale change to the tax system. Limiting compensation to a means tested \$3,000, which the person with a \$30,000 a year income gets nothing of, quite unfairly shifts some of the costs of tax reform to a group of people who do not deserve to be penalised in that way.

We would now like to address some of the broader issues of tax reform, Mr Chairman. The foregoing are the only specific, nimby type points that we bring before you. We believe that the government deserves full credit for its courage, and John Howard in particular for his courage and political acumen, in winning the recent election with a GST in his saddlebags. What should now be recognised is that the government, having been re-elected on a platform of tax reform, including a GST, has created a rare window of opportunity for the tax reform legislation finally passed to be real tax reform. The so-called new tax system documentation circulated during the election campaign falls a long way short of genuine tax reform. It was, and should be, viewed as nothing more than a politically astute GST sales package.

Effectively, the government's package really only replaces the wholesale sales tax with a GST. I do not know whether you have been given copies of the slides that we brought with us.

**CHAIR**—I only have your submission with the attachment, 'Savings exempt income: how will it work?'

**Mr Bricknell**—That is just three of the 20 or so pages that I gave to the secretary earlier. If you have a look at the first page of those three, these are slides taken from a Power Point presentation that we previously submitted to the committee, and we have given a copy on disk to you today. The GST, according to the government figures, in the year 2001-2002 raises \$31.96 billion. That principally offsets only the wholesale sales tax. The other taxes that are replaced are really quite insignificant. The only two that have any significance at all are the FID and BAD tax and the business stamp duties, and you note that is business stamp duties, not individuals. The franchise fee taxes are offset by increases in excise.

Given that increases in petrol, diesel, alcohol and tobacco excises, plus the luxury car tax and the wine equalisation tax, together raise \$8.04 billion, that is more than the reduction of \$7.04 billion in the current fuel excises. The above figures boil down to this: we are about to undergo enormous disruption to our entire taxation system just to abolish a couple of minor taxes, primarily on business, namely FID, BAD and business stamp duties. Where on earth is the logic in that? The government's tax package is of course laden with skilfully targeted bribes to buy the votes of politically significant sections of the electorate, and they largely rest on long overdue income tax cuts, but in fact one of the slides that I gave to your secretary, which I hope will be circulated to you, shows that Terry McCrann wrote in the *Australian* not very long ago, before the election, that the totality of the income tax cuts that are contained in the government's package adds up to exactly the amount that income taxes would have been cut by had indexation of income tax not been abolished.

So our proposition is, Mr Chairman, that the income tax cuts really ought not to be considered as part of the tax reform process. We believe they should be looked at in isolation, and that indeed if you take them out and you look at the income tax cuts in isolation the changes are really not much more significant than just offsetting the wholesale sales tax and a couple of other very minor taxes with a GST. That seems to be an awful lot of cost and an awful lot of pain to go through for such a small change. What we are suggesting to the Senate is that the political climate is now right for real, serious, thorough and comprehensive tax reform, and we would suggest to you that you could make any change to any sacred cow in the entire taxation system now and politically get away with it, no matter which party you come from. Therefore, we would suggest to you that, rather than scramble through a very limited, politically constrained tax reform package that was put forward by the government, by some artificial deadline, you take advantage of this current political climate and go for real and comprehensive tax reform.

We have provided some research to you. I personally spent two years heading up the National Seniors Association Tax Research Team. That was a member initiated organisation or group that comprised 55 members, and we spent two years looking at the experience of other countries with GST type taxes. We asked ourselves 20 questions about the GST—things like, ‘Is it a fair tax? Does it result in a reduction in the black economy? Does it increase the propensity to save?’ and all the other claims that were being made for a GST. We then looked at the experience of other countries to see whether in fact that experience supported any of those claims. I have to tell you that we were really quite surprised to find that overseas experience did not support a single one of those claims—not even one.

We have provided a summary of that evidence to you in a paper called ‘20 questions you should ask before you support a broad based consumption tax’ and we strongly suggest to you that you should ask those 20 questions and get the answers. Our resources were very limited. You have got far greater resources than us. We are suggesting to you that you use those resources to ask those 20 questions and get proper impartial answers to them. It is our view that those who propose major and wholesale change have the responsibility of demonstrating the need for the change. Frankly, we have not seen any evidence yet that suggests either that the current taxation system is beyond repair, or that a GST is the most effective solution to any one of the problems with the current taxation system.

The last point that we would like to make to you is that we believe you probably feel constrained in the amount of research you can do because of the time constraints that have been imposed on you, and the processes that you have to go through in selecting research consultants and so forth. It happens that I spent my 25 years in business as the founding chairman of a specialist professional project management consultancy. I am now retired from it, but the experience I had in that business taught me something that perhaps is not common knowledge amongst senators, and that is that the quickest and cheapest way to get any research done is in fact to engage a specialist professional coordinator or project manager, and give that person the job of inviting submissions and fee proposals and so forth, helping develop the brief for the study and so on, and then manage the performance of the study for you, whether it is a multidisciplinary team study or an individual study.

It is a very cost-effective way to do it. I am not pushing any commercial barrow because I am not in the business any longer, but it is an approach that the Senate could use to get

any number of studies done that it needs to get done in order to get to the bottom of the claims that are being made for the GST and to get answers to the questions that really should be asked before we introduce such a massive and major change. That is basically what we have to say.

**CHAIR**—Thank you, Mr Bricknell. Does your colleague Mr Funnell wish to supplement your remarks?

**Mr Funnell**—No, I do not, Senator.

**CHAIR**—Is it your wish that this set of slides or the document you have circulated be added to your submission for the record?

**Mr Bricknell**—Yes, please.

**CHAIR**—And is it your wish also that your document which I have not yet seen—‘20 questions you should ask before you support a broad based consumption tax’—which you have lodged with the secretariat also be added to the public record?

**Mr Bricknell**—Yes, please. In fact, I have given today’s presentation in writing on a disk to your secretary. I have also given on a disk the power point presentation, which only takes about half an hour, by the way, and it represents the summation of a couple of years of research, long before the Senate got involved with trying to research the GST, and therefore I recommend that you spend half an hour looking at it, and likewise the ‘20 questions’.

**CHAIR**—Okay, but it is your wish that they be included as part of your submission?

**Mr Bricknell**—Yes, please.

**CHAIR**—Is that agreed by the committee? It is agreed, and that will be done. You may have answered this, but can I just come explicitly to this point: you have raised a number of questions about the tax package that we are inquiring into and about the time scale in which we have to operate, and in which the Senate has to come to a decision. Are you putting to us that we should not proceed until such time as we have come to grips with the points that you have raised, or are you drawing those points to our notice irrespective of whether we proceed within our timetable or not?

**Mr Bricknell**—I think the answer to both questions is yes, to be honest. Our primary focus as an association is to suggest to you that you have a political opportunity that will probably never be repeated, certainly not in our lifetime, to undertake really thorough and comprehensive reform of the taxation system. Therefore, it ought not to be rushed. You ought not to be trying to complete it by July 2000. Indeed, you could argue that that year is a terribly bad year to introduce such a major change because we will still be recovering from the Y2K bug, and that putting it back for another 12 months is not going to hurt anybody.

**CHAIR**—Yes. What I am asking, though, is this: you have raised a number of objections to the current tax package. We may have to vote on these shortly. If your objections are not

met by the government, should we support the package or should we defeat it in the interests of getting a more comprehensive review of tax?

**Mr Bricknell**—It would be our view that you should vote against the package in its present form.

**Senator FERGUSON**—You will not have any problems with Senator Cook; he has already made his mind up.

**Senator SHERRY**—That is because we are smart like Mr Bricknell!

**Mr Bricknell**—We just think that the package is incomplete and it would be a mistake—

**CHAIR**—You will not have any problems with Senator Ferguson either. Senator Ferguson has the call.

**Senator FERGUSON**—I will pass it to Senator Gibson.

**Senator GIBSON**—Thank you, Mr Chairman. Mr Bricknell, isn't it true that on 3 October last year the government put a comprehensive tax package to the community and the people voted for it?

**Mr Bricknell**—Sir, not me. That is not my interpretation. I believe that there were opinion polls at the time of the election that were showing that 60 per cent or more of the electorate were still opposed to the GST but they just were not ready to vote a Labor government back into power, and on the basis of many other issues the current government was returned. I really do not believe that the current government was returned because it was offering a GST.

**Senator GIBSON**—We are offering a comprehensive tax reform program, of which GST is just one part, and the community voted. You in your submission congratulated the Prime Minister on winning the election with part of the tax package in his saddlebags.

**Mr Bricknell**—Yes.

**Senator GIBSON**—That happened, didn't it?

**Mr Bricknell**—Yes. But I do not agree that that is a comprehensive tax reform package.

**Senator GIBSON**—Okay, that is your view.

**Mr Bricknell**—Yes.

**Senator GIBSON**—But the government put a most comprehensive tax reform platform to the Australian community, the community voted, and returned the Howard government. Secondly, you also in your submission pursue Mr John McRobert's two per cent expenditure

tax proposal. Is it not also true that at the last election that proposal was taken up by the One Nation Party, and basically isn't it also true that they got nowhere in the election federally?

**Mr Bricknell**—It is a very interesting thing. This two per cent expenditure tax proposal has been around for several years.

**Senator GIBSON**—Sure.

**Mr Bricknell**—I first came across it when I was a member of the Australian Institute of Management Fellows Forum, and John McRobert was a guest speaker there, and he presented his thing and we all got copies of the book. The Fellows of the Australian Institute of Management at that time here in Brisbane were so impressed by the apparent logic of the argument that we formed a special working group, and we spent some months investigating this particular proposal. The Fellows of the Institute of Management are fairly senior managers. Our focus was to try to find the flaws in this two per cent expenditure tax proposal, and we could not find any. Our investigations showed that it stacked up. I understand it has also been subjected to some fairly rigorous analysis of the taxation modelling type by an academic, I think at a university here in Queensland.

We are not saying that the two per cent expenditure tax will work, but we are saying that it appears to us that it might work and that it at least deserves a very serious look. That is all. There was the nonsense of Pauline Hanson putting it up. I mean, Pauline Hanson could not understand it and therefore could not explain it, and of course it was doomed to fail in her hands. It is the sort of proposal that is very easy to scoff at and ridicule. The easiest way to get rid of it is to just scoff at it and say, 'It's ridiculous, isn't it, a two per cent tax. How could that possibly work?' The trouble is that, when you read the two books that he has written about it, it looks as though it does work. I am not expert enough to say that it does work. What I am saying is that the Senate ought to get someone—someone objective and impartial and qualified—to look into it in detail and see whether it does work.

**Senator GIBSON**—Mr Bricknell, are you aware that that form of transaction tax basically favours vertically integrated firms, so that, in other words, if Coles Myer went back and bought the farms and the quarries and all the way through the processing and transport and everything right through to the supermarkets, it would not have to pay expenditure tax on its transactions? The only expenditure tax would be on the final transaction.

**Mr Bricknell**—Yes, I am aware of that.

**Senator GIBSON**—So wouldn't that be to the disadvantage of all the small firms all the way along the line from the farms to the truckies to the processor to the wholesalers to the transporter to the retailer?

**Mr Bricknell**—Senator, I am really delighted that you have made that point, because that is exactly one of the strongest arguments against the GST. Right now, there are 70,000 businesses in Australia working as unpaid tax collectors for the government, collecting the wholesale sales tax—

**Senator GIBSON**—Mr Bricknell, I am not asking you about the GST. I am just asking about the expenditure tax which you raised in your submission.

**Mr Bricknell**—Sir, I am not here advocating the two per cent expenditure tax. Please understand that. I am simply saying that it looks as though it might work and it deserves to be seriously examined.

**Senator GIBSON**—Okay. Well, I have just raised a serious problem with you concerning vertical integration, which is one obvious point.

**Mr Bricknell**—Yes.

**Senator GIBSON**—The second obvious point is that people who deal in cash would avoid it. Isn't that true?

**Mr Bricknell**—Well, as they will the GST.

**Senator GIBSON**—No, they will not.

**Mr Bricknell**—No country in the world has been able to find a solution to the black economy and most countries with a GST have much bigger problems with the black economy than we have. Are you aware of the French scheme that was introduced to try and trap the black money operators over there after they had had a GST for a very long time? Are you aware that the black economy in Canada doubled after the GST was introduced over there?

**Senator GIBSON**—Canada made a mess of theirs; there is no question. But isn't it also true that in New Zealand the government was expecting 180,000 businesses to register in 1986 when the GST was brought in, but in fact 280,000 businesses registered, so there were a lot more businesses out there operating that chose to register in order to get input credits and also pay income tax.

**Mr Bricknell**—Yes, but hopefully your committee is having evidence placed before it to demonstrate just how easy it is for business operators to avoid paying the GST on at least some of their income, and indeed to collect the GST and not pass it on. Surely you are getting that sort of evidence from some people?

**Senator GIBSON**—Can I make just a final point about expenditure tax. Were you aware that European countries used that earlier this century and it was problems with expenditure transaction taxes which in fact led to the use of VATs in Europe?

**Mr Bricknell**—I think that it is very important not to confuse the expenditure tax with—I think it is the transaction tax, or there is another variation on the theme. I have seen a Treasury paper on the other one, and it killed it stone dead, absolutely. But the arguments that apply to that do not apply to the two per cent expenditure tax. And do not forget that the two per cent expenditure tax is the only taxation that is likely to address trading on the Internet. But, as I say, we are not advocating the two per cent tax; we are simply saying it deserves to be seriously examined. If it cannot stand up to rigorous analysis then throw it

away. But it just might, because the analysis that I have seen on it seems to suggest that it might.

**Senator GIBSON**—Transport costs: the government's proposed package, including a reduction in wholesale sales tax and a reduction in excise on diesel fuel, means on a Treasury estimate that road transport costs will go down by 6.7 per cent across the total Australian economy. We have had the Australian Road Transport Forum before this committee saying that for big trucks the costs are likely to go down by 15 per cent to 19 per cent. You were suggesting earlier today in your submission that diesel in fact was going up, but diesel excise is going to go down.

**Mr Bricknell**—No, sir. I refer you to page 100 of the government's package. It clearly shows that the take from various excises increases. It clearly shows it—your own figures.

**Senator BARTLETT**—You mentioned in your submission about the problem with specific compensation packages and the vulnerability of that. Do you agree that the best way to avoid that problem is to try and design a tax system that minimises the need for compensation?

**Mr Bricknell**—Absolutely. And that is going to be quite tough to do with a GST. As a matter of fact, anyone outside politics recognises the attraction of a GST to politicians, because it gets applied to everything and therefore there is less risk of individual pressure groups bringing pressure to bear on the people that have to legislate for it. That being the case, if ultimately this very blunt instrument is used, then the legislators really ought to err on the generous and high side in terms of exclusions from the GST. There was the nonsense last week about the scouts Bob A Job having to be subject to a GST—there are a million of those out there waiting in the wings to emerge when the GST comes in. Frankly, if the ultimate decision is to have a broad weapon such as the GST, then exemptions from it should be quite generous, because the alternative is to simply take the existing system and start applying it to a few services, with all the political pain, of course, that that involves.

**Senator BARTLETT**—In terms of the situation faced by investors—and you mentioned self-funded retirees, for example—the package as it stands at the moment changes the tax mix fairly significantly and increases indirect taxes. Do you believe that if that tax mix change was removed and the current balance was retained that would improve the fairness of the tax system and address the problems that your retirees have?

**Mr Bricknell**—No, we do not believe it will improve the fairness at all. I would ask the committee to have a look at this particular slide that I think you have a copy of. I think I just gave it to you. It is the last page in those three. The source of this is a CEDA report, from memory. This clearly shows that in Australia today we collect the same amount in goods and services taxes as is the average for the OECD. So, if we are not going to shift the emphasis more onto consumption and away from incomes and take ourselves out of step with the average of the OECD countries that have their GSTs, then we either have to increase the total tax take or we just rearrange the deckchairs on the *Titanic*—that is, we simply tax different goods and services—because right now we are collecting 31 per cent of our income, our total tax take, in goods and services taxes.

**Senator SHERRY**—I think you have rightly concentrated on the impact on people who are retired. There is one group you have not mentioned that I wonder if you have any view on or have considered in your studies, and that is the group of people in our society—and there is an increasing number of them—who effectively retire before the age of 65. They are either forced to because they are made redundant or, for their own lifestyle reasons, they get out before 65. I do not know whether you are aware or not that there is now a new requirement to deem your superannuation savings before you turn 65. We have had a substantial number of individual letters from these people to this committee, but they do not seem to be represented by any organisation, I think perhaps because of the sort of twilight zone that they are in.

**Mr Bricknell**—Yes.

**Senator SHERRY**—Have you any view about people in that position in our society? I understand there are at least 120,000 of them who have been hit by the deeming provisions on superannuation.

**Mr Bricknell**—Yes. Clearly, they are going to fall into this category of people who will be very badly hit by a switch of taxation from income to consumption, aren't they? Those people have got negligible incomes.

**Senator SHERRY**—They are dissavers, effectively.

**Mr Bricknell**—Yes, exactly. Believe me, you can go on and on. Read Austin Donnelly's book about all the people that you cannot compensate for a GST. There are thousands and thousands of categories of people whom you cannot adequately compensate for the introduction of a GST.

**Senator SHERRY**—Yes. As you said, for people who have paid income tax during their working life and then have retired, a significant switch in the system from taxing income to taxing consumption—vis-a-vis a GST—effectively means they are taxed on the way in and then they are taxed on the way out—

**Mr Bricknell**—That is right.

**Senator SHERRY**—Is that the best way of summarising it?

**Mr Bricknell**—Yes, that is our view. They are being retrospectively taxed for a second time.

**Senator HARRADINE**—I was going to ask a similar question to Senator Sherry. I am grateful that he asked it. Are you saying to us that there is nothing here in the government's new taxation system which goes near compensating self-funded retirees who choose to retire prior to the pensionable age?

**Mr Bricknell**—Yes, sir, absolutely. That is right. The compensation cuts out at—

**Senator HARRADINE**—Over \$30,000 it is, yes.

**Mr Bricknell**—Yes, and that is not a very high income. After that you get absolutely no compensation, but your standard of living is reduced by whatever amount your cost of living goes up and it effectively reduces your savings by whatever the net effect on your particular consumption pattern is—and it is probably something like seven per cent for that group of people; it could be higher in reality.

**Senator HARRADINE**—Your organisation represents those people, does it?

**Mr Bricknell**—Yes.

**Senator HARRADINE**—Do you feel that discrimination against self-funded retirees who retire early may be counterproductive in this period of high unemployment?

**Mr Bricknell**—I think it is unfair. Where is the case for suddenly taxing those people again? It really is irrelevant whether they retired before or after the nominated pensionable age, because the reality is that a person who gets to retire at 55 or 60 years has not got to that stage by having an easy life. They work extraordinarily hard and extraordinarily long hours. I have never met anybody who has been able to retire at 55 who has not really earned that retirement. Now, having earned the right to retire earlier, they have effectively said, ‘We’ll compress our working lives into a shorter period and retire earlier, and then hopefully get some rewards for that. You know, the time that we didn’t have with our children, et cetera, we might have with our grandchildren,’ and then they expect a certain standard of living because they make the decision to retire at a certain level of savings; not necessarily millionaires, you know.

Once they have retired with that level of savings and left their businesses, sold their businesses, left their employment—whatever—there is no way in the world they can go and top it up again if someone comes along and says, ‘We’re going to take seven or eight per cent off the top of your savings.’ So, if the government is going to introduce a taxation system that really does have the effect of taking seven or eight per cent off the top of the savings of people in that category, then it ought to compensate them to the full amount so that they can just stay where they are now. No-one is asking for a better deal; just leave them where they are now.

**Senator CONROY**—I want to follow up on that point which you articulated:

Most of the goods and services consumed by people in their latter years are not currently taxed under the Wholesale Sales Tax system.

That is the nub of the compensation question, because the government has tried to argue that the increase in prices is only 1.9 per cent and it has made a range of assumptions about that.

We have had other organisations come before us to argue that the package impacts on the people they represent quite a lot more than 1.9 per cent, on the same argument. Have you got any surveys or studies which point to the sort of expenditure patterns of the people that you are representing? Trying to argue that because the price of a fridge is going to go down, someone that you are representing is going to run out and buy a new fridge and therefore they are going to make all this notional saving is palpably nonsense.

**Mr Bricknell**—Yes. I said before that it is up to those who are proposing dramatic change to demonstrate the need for the change, and then to try and identify its impact on all those who are going to be impacted, and then give those people a chance to look at the compensation to see whether it is going to be adequate. I do not believe that the task rests with us, with our limited resources, to go out and do studies and say, ‘Hey, this particular group is going to get really seriously impacted in a negative way by this tax change.’

However, you do not have to be a rocket scientist to work out that, if you are at the latter part of your life and you are no longer buying a whole lot of capital goods, you are no longer buying furniture and cars and goodness knows what else to a large extent, but instead you are buying things like food and holidays and movie tickets and stuff like that—

**Senator SHERRY**—Videos.

**Mr Bricknell**—You just have to look at the wholesale sales tax list and see how many of those items are not taxed. So, clearly, one of the studies that the Senate committee needs to do or commission is to have a look at different groups of people, specific categories of people like that, and say, ‘What is going to be the real effect on these people?’ and then let us have a look at the compensation that is proposed, because, if the argument being put forward by the government is that we are going to have no net increase in the total tax take, then for every winner there has to be a loser by definition, and we just need to know who are going to be the losers and what compensation is going to be given to them, because the compensation should be full, shouldn’t it?

**Senator CONROY**—Absolutely.

**Mr Bricknell**—It should be full compensation for the impact if there is to be no net change in the total tax take.

**Senator CONROY**—Would you believe that the Treasury or the government should have commissioned this sort of study?

**Mr Bricknell**—Yes, of course I do. But at the end of the day the taxpayer is going to pay for it, whether they did it before or after the election. Our key point here is that it is great; you have an environment now in which you can really undertake proper tax reform. I am saddened to see party politics still being played and I think it is fair enough that it is played out in the open, but behind closed doors I would submit to you that you people should be trying to work out an approach to real and thorough tax reform, not the half-baked proposal that we had before us at the election.

**Senator CONROY**—This committee through the Senate has actually commissioned a range of distributional amounts to try and get to this point to assist with that debate. Unfortunately the terms of reference of this committee are into the government’s tax package. We do not have the capacity to go and do anything we want. We are constrained by the terms of reference that were passed by the Senate, and that limits our capacity. We have been able to commission some of that work that I talked about, but we do not have the capacity to just investigate whatever we would like. The committee is funded by the Senate and it has a range of constraints.

**Mr Bricknell**—But that is a self-imposed constraint by the Senate on itself and I am suggesting to you: get the party politics out of it and get into a huddle behind closed doors and say, ‘Look, let’s take advantage of this window of opportunity to have real and comprehensive tax reform, which may or may not include a GST. Let’s seriously look at what the real problems are in the tax system and what the best solutions to those problems are.’ This is a God-given, once in a lifetime, opportunity. You should be taking it.

**Senator FERGUSON**—Senator Conroy is used to being in a huddle behind closed doors, Mr Bricknell.

**CHAIR**—That is an unnecessary intervention, but I think we have concluded our questions from the committee. Thank you, Mr Bricknell and Mr Funnell, and I am sorry that you have had to hold the floor, Mr Funnell! Thank you very much for aiding the committee. The committee is now adjourned for morning tea.

**Proceedings suspended from 10.48 a.m. to 11.05 a.m.**

**ELLIOTT, Mr Philip Gregory, Chief Executive Officer, National Credit Union Association Inc.**

**WEATHERLEY, Mr Derek Ross, Research Assistant, National Credit Union Association Inc.**

**WILSON, Mr Fred Albert, Director, National Credit Union Association Inc., and Manager, Queensland Police Credit Union Ltd**

**CHAIR**—I welcome the representatives of the National Credit Union Association Inc. I presume, Mr Elliott, that you are leading on behalf of the organisation?

**Mr Elliott**—Yes, that's right.

**CHAIR**—As you have no doubt been informed, we would invite you to make a short opening statement addressing your submission, and then be available for questions from the committee.

**Mr Elliott**—Thank you very much for this opportunity to address the committee. We certainly do appreciate it, and appreciate the fact that such a committee has been formed to review the matter of the goods and services tax. From our perspective, a primary concern is that the application of the GST is uniform across all financial institutions, and the credit unions and the members do not incur disproportionately higher GST costs.

Today our purpose is to explain and highlight the inequities which would apply to credit unions if the GST bills were passed in their present form. These inequities arise largely because the legislation fails to recognise the different structure of the credit union system which has been developed over the past three decades in Australia, and that has been due to the small size of individual credit unions. Additionally, the definition of 'financial supply' has consequences for all financial institutions because, as presently defined, it would result in a less efficient financial system, and would particularly disadvantage smaller financial institutions, which, from our perspective, of course includes credit unions.

In order to appreciate the significance of the concerns we have about the application of the GST to credit unions, it is important that the government understands how credit unions are structured in Australia and how that structure differs significantly from the banks. The Australian credit union system contains 247 individual credit unions. They have total assets of approximately \$19 billion, and they have 3.5 million members. Credit unions are small financial institutions averaging only some \$62 million in total assets. Reference to appendix 1 to our submission details those statistics. That is in comparison to the average size of a bank in Australia—some \$34,323 million in total assets. That is more than 550 times the size of the average credit union. The largest credit union is approaching \$850 million in Australia, while the largest bank is some \$210,000 million in total assets. So the size scale is significant in this issue.

Major banks, therefore, have the internal resources necessary to provide a very diverse range of services through their branches and to their customers, such as training, data

processing, marketing, cheque clearing, ATM networks, POS facilities, home banking, and electronic funds transfer. It is virtually impossible for most credit unions acting alone to provide similar services to their members on a competitive basis. In many cases, due to their size credit unions acting alone would not be able to provide most of these types of services. This size differential creates the requirement for credit unions to act collectively in so many areas of their operations.

As a result of that, credit unions have historically banded together to undertake many of their transactional and processing services, and formed cooperative credit union service organisations that we refer to as CUSOs, and I will use that phrase from here on. These CUSOs, which are owned by a group of credit unions, enable them to act collectively to achieve the economic scale required to in fact deliver many of these retail services that are so essential to consumers today. Without the CUSOs the service capacity and competitiveness of credit unions would be enormously impaired. We would like to suggest that a direct comparison can be made between the structure of a large financial institution, such as a major bank with all of its branches, and the credit union system structure that has been described in our submission. Services provided within one corporate body by the head office to the branches of a large financial institution are identical to those shared among many credit unions as separate corporate entities in the credit union system. The diagram at page 3 of our submission illustrates those similarities between the two structures and the basis under which GST would be considerably higher proportionately for credit unions than for the banks.

In essence, there is no difference between the many services transacted by CUSOs with credit unions and bank head offices with their branches. However, under the proposed GST legislation the provision of services within the credit union system would be subject to GST while the same services within a bank structure would not be. That is simply because the credit unions are separate legal entities, not branches.

On page 4 of our submission we detail the theoretical GST comparison costs for computer facilities if a bank and a credit union were to spend \$5 million on hardware and \$5 million on software. It shows a once-off GST cost of \$500,000 for a bank, but for the credit unions it would be a first-year cost of \$1.2 million and then an annual ongoing cost of \$200,000, simply because GST is being applied at multiple stages.

This structural problem in relation to a GST was encountered by our credit union colleagues in Canada almost 10 years ago. But that inequity problem was resolved through the Canadian government's recognition of the special credit union structure and, very briefly—we would not want to attempt to address it at this point here—the GST grouping was the methodology under which they achieved that. We appended to our submission the publication by the Revenue Canada Customs and Excise regarding GST and its application to credit unions. I would like to make one quote from that paper. It states:

Generally, the GST applies to all taxable supplies between two legal entities including those involving related members.

It goes on to say:

The organizational structure of the credit unions would, in the absence of special rules, result in the application of GST to the charges for training seminars provided by a central credit union to a local credit union, because the central and the local are two separate entities. Where the recipient of a taxable supply is engaged in exempt activities, such as a credit union, this may result in non-recoverable tax since input tax credits would not normally be available for tax paid by the recipient.

To summarise, the position that they adopted in Canada in recognition of this problem was:

If credit unions A, B and C own 100 per cent of X Ltd, X Ltd is considered to be closely related to each of A, B and C. X Ltd is also considered closely related to all other credit unions in Canada. As a result, X Ltd may elect with credit unions A, B and C and all other credit unions in Canada, pursuant to subsection 150(1), to have all taxable supplies between them exempt. A separate election would have to be filed jointly between X and each credit union.

We submit that as a precedent in relation to this difficulty, and also the solution path in that regard. That is the first arm of our concerns.

The second concern is with the actual definition of 'financial supply'. At section 40(5) it includes 'the creation, keeping or closing of savings, deposit and cheque accounts and loan transactions' and they are to be exempt from the GST. However, a savings, deposit or cheque account is not an inert item and is, by its very nature, a series of debit and credit transactions. We argue that the processing and recording of such transactions constitutes the keeping of the account. It would be hard to keep an account without recording all of those activities. In this day and age, there are enormous bases for generating transactions from ATMs through to remote point of sale transactions as well as over the counter, as you would be aware.

So we are proposing that to exempt the keeping of a cheque account from GST, whilst subjecting the institution to GST on fees it incurs as a result of the account holder's transactions on the account, is unfair and not quite logical. To be consistent, direct charges incurred by the financial institution for transactions, which we submit are the very essence of keeping the account, should also be exempt. To draw on a very detailed example, where a member of a credit union uses a bank owned ATM to withdraw money from a savings account, the credit union will be charged the fee by the owner of the ATM and GST would be payable, for example 10c on a \$1 withdrawal fee.

Because a withdrawal fee charged to another financial institution is not considered a financial supply, if the credit union then charged the member the same fee of \$1 for the transaction, it is understood it would be deemed to be a financial supply and therefore GST could not be applied to it, so the credit union would be wearing the GST with no way of recovery. This same scenario is replicated in all instances where a financial institution incurs a fee for a customer initiated transaction, whether it be cheques, EFTPOS, direct entry, ATM and so on.

And then we get a broader issue that we would appreciate the committee address. It is that the technology infrastructure exists in Australia to allow consumers to choose their financial institution, irrespective of its size, and have access to almost any electronic transaction facility in the country. To introduce GST on these networks effectively creates a disincentive for their use. It inhibits the efficiency of the financial system as a whole, and it will inconvenience consumers and disadvantage small financial institutions in particular.

Further, substantial benefits would accrue to the owners, usually the larger institutions, of such transaction facilities as they would be exempt from GST when their customers transact, and they are also able to claim input credits when charging other institutions. For example, the Commonwealth Bank has an extensive ATM network and its customers can access some 2,500 ATMs and 83,000 EFTPOS terminals. All such transactions would be GST exempt when transacted by a Commonwealth Bank customer but GST would be payable when a credit union member transacted on one of those devices. To further illustrate the significance of the structure in Australia, banks own 7,828 of the 8,698 ATMs in Australia while credit unions own 348 ATMs, so it is a scale issue.

If smaller financial institutions are penalised by the application of GST from having access to this network, their ability to provide competitive financial services would be significantly impaired. Again, our credit union colleagues in Canada faced this very same problem at this stage of the GST development in Canada. While the Canadian definition of financial services for GST-exempt status reads very similarly to ours in relation to savings, chequeing, deposit and loan accounts, et cetera, it was expanded to include charges for transactions on accounts and specifically for ATM transactions.

Credit unions are assisting many people in the community and they are moving into remote areas not serviced or that have been vacated by the banks—and there has been a lot of publicity about that in the last few years. It is the very structure of credit unions, which is very different to the banks, that facilitates this. Credit unions are driven by the local membership and the board of directors that is derived from that membership, as opposed to the bank structure which you are all familiar with. Surveys of consumer satisfaction with a financial institution in recent years have recorded very high satisfaction levels with credit unions and poor to low levels with banks. Again, it is because of the very structural difference in the corporate nature of credit unions that is producing these sorts of results compared to the banks. But it is also the reason why we have this problem with the GST. We are different and we are not in the corporate mould that the GST was obviously designed around.

We would submit it would be very unfortunate if these same credit unions were significantly disadvantaged compared to the major banks by a government taxation policy which was not flexible enough to treat credit unions equitably. All we are asking for is to be essentially treated under the GST in the same nature as a bank. In essence, if you took the Commonwealth Bank and looked at its head office, subsidiaries and all the branches and then did a similar pick with credit unions and had the service organisations that they have developed, and then all the credit unions listed under that, on such a grid system it looks very much the same as a bank. But the tragedy under the GST proposals is that every time a credit union transacts somewhere, because it is a separate legal entity, it will be incurring GST and therefore be significantly impacted upon as a result.

I would like to pass now to my colleague Derek Weatherley to address three other areas in relation to the GST, and that will be the conclusion of our presentation to you.

**CHAIR**—Thank you, Mr Elliott.

**Mr Weatherley**—Briefly I would like to highlight a couple of important points in relation to inequities which arise between large and small financial institutions due to the input credit system. Firstly, the availability of input credits and the computation of input credits may be a factor which distorts competitive balances between large institutions and small institutions. We know that all financial institutions will be required to allocate purchases of inputs into those which are used to provide taxable services, zero-rated services and input-taxed services. The GST paid on inputs which are used to provide taxable and zero-rated services will be refundable as an input credit. The GST paid on inputs which are used to provide input-taxed services will not be refundable and will be borne by the financial institution.

The inequity arises because most credit unions will have no taxable revenues and, as a result, input tax credits will be virtually non-existent for credit unions. Banks, on the other hand, will have more substantial taxable revenues and therefore will have the opportunity to claim significant input credits. We can fairly assume that in calculating their input credits banks will do all they can to allocate a maximum amount of expenditure to taxable activities, thus minimising their GST burden. All we ask is that this be recognised and that the legislation be tight enough to prevent undue input credits from being claimed by banks. If this is not done, smaller financial institutions may be disadvantaged.

My second point is in relation to services provided by banks to credit unions. Under the legislation as it stands, a credit union must pay GST on many of the services provided to it by a bank but will not be able to claim the input credit for the GST paid on that service. The bank, on the other hand, will be entitled to claim input credits for all GST paid on inputs involved in providing these services to a credit union. This inequity further tips the scales in favour of large financial institutions. This would be resolved by expanding the definition of ‘financial services’, as was earlier mentioned by Philip.

The next point is just a brief one in relation to the Wallis inquiry. The Wallis inquiry sought to achieve a number of objectives. Among these was to introduce greater competitive neutrality across the financial system and establish more contestable, efficient and fair financial markets, resulting in reduced costs to consumers. The Wallis report also noted that a more competitive and efficient financial system can be promoted by regulatory and taxation arrangements designed with greater regard to their effect on competition and administrative efficiency. For the reasons which we have outlined today, it is fair to say that the GST bill in its current form runs counter to these important goals as far as credit unions and most small financial institutions are concerned.

The final point I would like to make is on outsourcing. The Wallis report says that outsourcing has the potential to lower industry costs and remove an existing barrier to entry for new competitors. A major impact of the GST bill in its present form is to penalise outsourcing by subjecting it fully to GST. This imposes a major disincentive to financial institutions to outsource and prevents financial institutions from providing the most cost-efficient services to consumers. Our main concern here is that it imposes a more substantial disadvantage on smaller institutions because many of them must outsource to enable them to compete effectively in today’s markets.

In conclusion, I would like to summarise the changes that we believe are required to restore equity to the legislation, and these were mentioned earlier by Philip. I will just quickly go over them again. Firstly, we would ask for a recognition of the credit union system. The legislation should provide that the supply of goods and services between credit unions and their jointly owned service providers are not subject to GST. This would recognise that such transactions are identical to the provision of goods and services by the head office of a large financial institution to its branch network. As Philip mentioned, this recognition was granted by the Canadian government when it introduced a GST in 1991 and supplies between credit unions and their various service organisations were effectively exempted from GST.

Finally, we would ask for an expanded definition of 'financial supplies'. The current definition of 'financial supplies' includes 'the creation, keeping or closing of a savings account, cheque account or deposit account'. The legislation is not precise on the scope of this definition and is open to interpretation, as the definition does not include transactions which by their very nature constitute the keeping of these accounts. The Canadian government also recognised these transaction activities as financial supplies and accordingly included them in their definition of 'financial supplies'. We ask that a similar recognition be given in our legislation.

**CHAIR**—Thank you. I wonder if you can answer this question. You have mentioned where you want the current bills that are before us to be changed. If they are not changed, do you want us to support the legislation in its current form or to reject it?

**Mr Elliott**—That is a very broad issue, because you are basically addressing the question of the whole issue of a GST. Because of the significant disadvantage that credit unions would suffer, I think we would have no alternative but to ask for the GST bills to be defeated. We are not proposing that you would see the adjustment as a much more reasonable course, but the impact is significant. It is following on the heels of the removal of a taxation exemption that the credit unions had, which was also supposed to be on the basis of introducing a level playing field. Unfortunately, again because of the different structure of credit unions which really was not recognised by government in our opinion, credit unions are disadvantaged because the level of post-tax profit, which is their only method of capitalisation, is only two-thirds of what it used to be and the tragedy for credit unions is that they are unable to utilise franking credits because they are prohibited from issuing permanent shares.

We have got a similar problem with the GST proposal as we have with the existing income tax, whereby government thought it was producing a level playing field but it did not look close enough to say, 'Oh, credit unions are mutuals. They don't have permanent shares on which dividends can be paid which are fully franked,' or at least partially franked. So the credit unions have got franking credits now locked up in them. Their capital raising ability in the previous period where they were tax exempt was a third again of what it is, so it almost appears as though the danger sits of a lack of recognition that there is something different about credit unions and that something needs to be adjusted.

**CHAIR**—You mentioned the notorious problem of banks leaving town in rural Australia and leaving country townships without a bank or a financial institution of any sort—or at least a long way from one—and the credit unions are beginning to fill that gap.

**Mr Elliott**—Yes.

**CHAIR**—You may wish to take this on notice. Do you have any figures about that trend? To what extent are credit unions beginning to fill the gap?

**Mr Elliott**—The last figures I saw, which are probably a good six months old, indicated about 43 different areas, principally in the three eastern states, where credit unions had moved in to provide some branching facility for local communities. It is not always the case where a bank has moved. There have also been a small number of cases—seven or eight—where there was no local facility at all and the local community raised the issue and drew it to the attention of credit unions and they have moved in there.

In terms of the total number of credit unions—240-odd in Australia—for them to have gone to 43 or 44 different sites in the last four years or so and created a facility for financial services that did not exist previously or that had been removed, we consider a remarkable achievement. Given the overall small size of credit unions and, as I said, their small number, we think that is quite remarkable. The impact of the GST, as proposed, could only have a very serious impact on their ability to continue to do that sort of thing in the future, let alone their current operations.

**Senator FERGUSON**—If I heard you right, Mr Elliott, you said that if your recommendations were not accepted, you would feel inclined to ask senators to oppose the GST bills. Does that mean that you also want senators to oppose the income tax cuts? Do you want the senators to oppose the reduction in fuel excise? Do you want the senators to oppose the removal of all of the other taxes that are currently in the package; in other words, you want the whole package rejected?

**Mr Elliott**—In the way the question was phrased, I guess it gives us little opportunity to respond in any other way than that, simply because the negative impact of the GST on credit unions compared to the larger financial institutions would be so substantial as to cause serious problems.

**Senator FERGUSON**—In general terms are you in favour of the tax reform package or against it? We are not talking about a GST. This is an inquiry into a new tax system; it is not an inquiry into a GST.

**Mr Elliott**—No, we are not opposing it at all. To some extent, we are fairly neutral on that issue. We will let individual members of credit unions decide how they would react to that. Largely, we are neutral on it. The government has proposed it; the bills have been presented. We are not proposing any action to oppose the bills per se. Our position is fairly narrowly in relation to the direct and immediate effect on credit unions, so our preferred path—the only path that we have contemplated in relation to our reaction to the GST—is to seek these areas of change.

**Senator FERGUSON**—It is a fact though, isn't it, Mr Elliott, that currently the application of GST to financial services is still a matter of ongoing consultation with Treasury, and they are meeting with industry representatives now?

**Mr Elliott**—Yes, and this is one of the many forums that credit unions are using to get their viewpoint across and, hopefully, have it accepted.

**Senator FERGUSON**—So there are still ongoing consultations?

**Mr Elliott**—Yes.

**Senator FERGUSON**—It is not something that is cut and dried.

**Mr Elliott**—No.

**Senator FERGUSON**—In fact, I think it is probably fair to say that this government has been rather helpful to the credit union sector recently, with the issuing of cheques, direct access to payment systems and those sorts of things. They have all been introduced. So you could hardly say they have been unsympathetic to credit unions.

**Mr Elliott**—We are certainly not saying that. The only other reference I made was in relation to the removal of the tax exemption, which has had an adverse side effect and which we can only explain on the basis that that difficulty was not anticipated because the structure of credit unions was not fully appreciated.

**Senator FERGUSON**—If the recommendations that you are asking us to put in place come to be, is it possible that will increase the cost of financial transactions to your consumers?

**Mr Elliott**—If these proposed amendments or our requests are adopted?

**Senator FERGUSON**—Yes.

**Mr Elliott**—With the removal of FID and BAD it probably means that the cost to the credit union members could reduce.

**Senator FERGUSON**—You also spoke, I think, in your submission about banks leaving rural areas.

**Mr Elliott**—Yes.

**Senator FERGUSON**—When did banks start leaving rural areas?

**Mr Elliott**—I am no authority on that, but I suppose it could be as far back as 15 years ago that branches were being closed. It is obviously in the last five to seven years that the volume of branch closures has accelerated under the banks.

**Senator FERGUSON**—Fifteen years ago. This is not a dorothy dixer, but that just about coincides with the advent of the Labor government in 1983, and if that was when they started leaving rural areas in droves, what action was taken during that period to try and retain banks in rural areas?

**Mr Elliott**—Are you talking about by local communities?

**Senator FERGUSON**—Yes.

**Mr Elliott**—I really have no technical knowledge on that.

**Senator FERGUSON**—Or by governments, previous governments particularly.

**Mr Elliott**—As I say, I have no expert knowledge on it. My observation would be that very little was done. It was, I guess, like train tracks being pulled up in certain areas; people accepted that was the way it was and went on about their lives. But attitudes today are a bit different. Fred Wilson would like to comment on that.

**Mr Wilson**—I think it is important to understand the differences between the banks and the credit union industry per se. Fifteen years ago the banks were going through an economic decision making process where, for pure business purposes, they decided that it was uneconomical to keep remote branches open. Credit unions, however, operate on a completely different philosophical basis. Our credit unions operate on the basis that we exist purely to service our members. We are not driven by the profit motive, which you will find that most of the major banks are. Therefore, the issue of providing service is uppermost in our minds, as opposed to making profits, and I think you will find that most of the bank closures have been profit driven.

**Senator BARTLETT**—You mentioned that you are having ongoing discussions with Treasury about this. I suppose it is a bit hard to give a precise answer, but what is your general perception of that? Are you reasonably encouraged by the reception you have been getting?

**Mr Elliott**—Yes, the reception is probably comforting but a long way short of a commitment to redress these issues.

**Senator BARTLETT**—And to actually address the main concern you have got would require an amendment to the legislation that we are examining?

**Mr Elliott**—Yes.

**Senator BARTLETT**—So it is not something that could be done by a bureaucratic ruling down the track or whatever?

**Mr Elliott**—No, it is fundamental to the application and definition of ‘exempt suppliers’.

**Senator BARTLETT**—Okay. You have mentioned a number of times the Canadian government approach and addressed it in your submission as well. You are saying that the specific approach that Canada uses would completely address the concerns you have?

**Mr Elliott**—Yes. We were absolutely amazed when we communicated with our Canadian colleagues knowing that they had had a GST for almost 10 years to find that the same two major problems that we had identified had occurred with them, and that they were addressed fairly easily in terms of definition in relation to the Canadian legislation.

**Senator BARTLETT**—You may need to take this question on notice. You have mentioned the current definition of ‘financial supplies’ that is in the bill. Would you be able to provide us with specific wording that you believe we should put in place. It is one thing for us to recommend an in principle change, but we do need to have a specific change.

**Mr Elliott**—We would be only too happy to assist in that regard.

**Senator BARTLETT**—That would certainly be handy, from my point of view.

**Senator HARRADINE**—We got that in Adelaide, I think.

**ACTING CHAIR (Senator Ferguson)**—I think we may have got some of that information but I am not sure that we got all of it, Senator Harradine. But perhaps we could just check the record and make sure whether that request was made before. Senator Bartlett was not there.

**Senator CONROY**—If the parliament does not adopt your suggestions, how serious an impact is it going to be in terms of the viability of the individual credit unions?

**Mr Elliott**—Credit unions have always demonstrated a remarkable resilience, but I will try to put this into perspective. As you would be well aware, the capital adequacy requirements for financial institutions are fairly significant and, in crude terms, to move away from the risk weighted eight per cent, given the balance sheet of the average credit union, the credit union has got to have \$5 in capital for every \$100 it takes in on deposit over the counter and then lays off in loans to members or what have you. That is the simplest way I can put it.

Credit unions can only do that with post-tax profit at the moment. Going back, four years ago they could make a profit and the whole lot could be put to form their capital. Now, for every \$5 we used to get there we are only getting about \$3. That means that the ability to grow is impaired, so we are still grappling with that problem. As a result of the taxing of credit unions, credit unions are very seriously looking at the notion of issuing permanent shares. They are not allowed to under the law at the moment, but that is being looked at at the moment as well.

With that severe limitation on growth and profitability, the aggregate level of profit of all Australian credit unions last year—and they are the most highly capitalised financial institutions in the country, far better than banks, at about 14½ per cent risk weighted—an approximate \$40 million GST, which is the estimated load credit unions would carry because

there is very little input credit available to them, would consume something towards 30 per cent of the total annual profits of credit unions in Australia. So in terms of the significance of the impact I think that is a fairly substantial illustration of it.

**Senator CONROY**—Does that start moving down towards your problems with your capital adequacy?

**Mr Elliott**—Yes. What it means is that if that much higher level of cost is to be borne by credit unions, the level of profit left over is going to be less. Therefore, the amount they can appropriate to capital will be less, which means they will not be able to grow as much. There is a limiting cap on growth by the level of capital that you have. So in terms of federal revenue, if the issues we are talking about do add up to \$40 million it means nothing in overall terms, but in the bottom line impact on credit unions they have enormous ramifications. I certainly would not say life threatening. But one of the other options would be to just pass that sort of cost on to the members, but then you move into the dangerous area of not being cost-competitive, and it would be as a result of credit unions paying so much GST on the same things that banks are not paying GST on.

That really is the essence of our argument. It is the inequity: that simply because credit unions are built differently they would be wearing the GST. And we are certain that is why the Canadian government responded the way it did. It said, 'We don't want you to be unfortunate because you are built more consumer friendly. We'll recognise that and say you can go this way and the banks can go that way, but there should be neutrality in terms of the application of GST.'

**Senator CONROY**—Are there alternative sources of revenue for you?

**Mr Elliott**—Not really, no. Credit unions are very narrow in the range of services provided to members. They do not have the breadth and plethora of national and international activity of the banks, for the fairly obvious reason that so many credit unions are dealing with consumers on consumer issues and they are not into the corporate side of activities. So to keep supplying the services that the members of the credit unions want, they are still very much in a narrow band of services. Financial advice is an area that is certainly creeping up in credit union activity in more recent times, but again that is because more of the members are looking for that sort of service.

**Senator CONROY**—If you do cop a 30 per cent hit on your profit would you have to look at introducing fees and charges?

**Mr Elliott**—Yes.

**ACTING CHAIR**—As the committee has no further questions, thank you very much for appearing before us today.

**Mr Elliott**—Thank you very much.

[11.43 a.m.]

**JEREMY, Mr Richard Keith, General Manager, Australian Beef Association Ltd**

**McGOVERN, Dr Mark, Economic Adviser, Australian Beef Association, and Director, Rural Policy Institute**

**ACTING CHAIR**—Welcome. I invite you to make an opening statement.

**Mr Jeremy**—Thank you. I will begin by saying that apart from managing the Australian Beef Association I am a cattle producer in my own right, and have been for quite some time. The Australian Beef Association Ltd is the only national beef-specific organisation that counts amongst its members cattle producers, feedlotter, agents, transporters, abattoirs, butchers, and even one of the major supermarkets—so we are beef specific from top to bottom. That is why we are somewhat distinct from other farm and rural organisations that try to cover a wide range of farming or some organisations that only cover one sector of a production system. So my experience and my comments will stick to the practical matters of beef production, and Dr Mark McGovern will deal with the more complex issues as an economist and talk percentages and all those wonderful things that you learned gentlemen probably understand far better than I do, whereas I am much more on the practical end of the business. So item 1 on our submission is fairly complex about price elasticity, and he will take those matters when you are ready with your questions.

Items 2 and 3 of our submission are self-explanatory—I have not got a lot to add to those. But regarding item 4, we find that with further examination the pay-as-you-go tax has the potential to severely affect cash flow. Producers are forced at times to sell large numbers of cattle, due to drought, or perhaps they sell their property or such things happen that they can get a surge of income within one quarter. Whereas in times gone by that has been averaged out over the year and the next year, as I understand it in this case your tax will be payable immediately. That could create a cash flow problem over the following period of time, particularly if you are running into drought or something like that.

In talking to my own accountants—they have done GST workshops and summits and so on—they believe that the quarterly tax return, added to the GST return quarterly, will have to be a very accurate document because the tax is payable on that—so this really means that I will have to do four tax returns per year. What concerns me is the compliance cost of that. It is fairly normal on a farming enterprise such as mine to pay about \$2,000 to get your income tax done up—with all the intricacies of the business—so it is quite possible that my accountancy fees will rise to \$8,000 a year. So there is quite an impost there on compliance.

Regarding item 5, a prominent Queensland exporting meatworks spokesman has advised me that keeping track of where the product of a beast ultimately is consumed is virtually impossible because a domestic carcass may have the hide, tallow, and meat meal exported and an export carcass may in fact have the hide used domestically. One major abattoir has advised me that it has a computer system that can keep track of that. Another major export abattoir advised me that it is very doubtful and some other system would have to be devised to be fair if they are to determine when they pass the GST back to a producer or when in fact they do not have to, as is the case with exports.

I have heard, and a good senator rang me at one stage and advised me quite clearly, that the proposed reduction in the price of diesel coupled with other transport savings, say the reduction in sales tax from 22 per cent to GST of 10 per cent, will mean that the transport costs in my business will be substantially reduced. I am also advised by the New South Wales Livestock Transporters Association that due to the already difficult financial position in this industry that they will be unable to pass on any reduction in cartage costs to keep themselves afloat, to keep themselves viable. Really that is a business decision for them. It is something we really cannot propose legislation on saying that transport costs will or will not come down. They will gain those savings, and I would think the transport industry would be fairly happy about the GST, but there is nothing to say that that can be passed on to us in the way of reduced charges.

To take a live instance, my chairman John Carter sent me a letter relating to his own business where he paid \$16,000 in transport costs last year. If in fact his cartage costs did reduce by 10 per cent, it would mean that he saved \$1,600. Yet in the total expenses of his whole business, with \$205,000, he really feels it is very much a tiny amount compared to all the other problems that will arise because we pay GST and the compliance costs of it.

There are two or three matters that have come to my attention in the last day or so that are not raised in our submission, and I would seek the committee's permission to have the other few things I am going to say typed up and forwarded to you if that is possible. The real fact is that the primary producers, and particularly beef producers, are price takers, not price setters. While it is relatively easy for somebody in a jeweller's shop or an accountant or somebody else to say, 'This is the price and there's 10 per cent added on,' in the case of the primary producer, or particularly the beef producer, that simply is not possible.

The fact of life is, more particularly in Queensland than anywhere else, that when producers sell their property or are placed in a situation where they need finance, or perhaps they are facing a drought and run short of feed, they have to take their cattle to the saleyards and take what they get for them. If you do not go through the saleyards you have to go to the abattoir or the major meatworks and say, 'I've got so many head of cattle ready. What are they worth?' and they tell you what they are paying, and that is that.

The buyer in every case will be running to a budget. A major export meatworks, for instance, tenders for the Korean market and he tenders for the Japanese market. If he has won the tender he knows exactly what he can pay for cattle, and it is obvious that if a 10 per cent GST is in place, he will simply have to reduce his bidding price, whether it is through saleyards or by negotiation, by an amount equal to the GST so that his total input cost is still the same. Just to give you a simple example, if an export heifer is worth \$300 to the abattoir, and it is going to be an export carcass, there is no way he can suddenly pay \$330 to make anybody happy. He will have to reduce his bid price, or his negotiated price, to \$270 plus GST, so that he still comes out with a \$300 input cost.

It is the same thing in the stud game. I am a stud producer. If I put a line of bulls in the sale for sale to other producers, if somebody has got a budget of \$10,000 for bulls this season that is what his budget is—it does not suddenly and miraculously become \$11,000—and we have to take it. The bid would become \$9,000, the GST would be added: his budget is fulfilled, my income is reduced. It is that simple.

It is our contention that nothing proposed in the tax changes so far can compensate us for a 10 per cent drop in gross income. I know that there are other taxes going to be removed, I know that it will be fiddled about with, but the beef industry is already in a nonprofit situation—and that is supported by figures from ABARE. To take another 10 per cent of our gross income, even if it worked out a little better than that, we simply have not got it to give. It is that simple.

Another point that was brought to my attention only last night relates to the sale of a farm. Correct me if I am wrong but, as I understand it, if a business is sold as a going business—lock, stock and barrel—it is GST free. But in the case of farms, probably nine times out of 10 the land is sold separately. The buyer, for reasons of his own, either does not want your breed of cattle or is not interested in your old machinery or has machinery of his own. Whatever happens, normally you could not call farms a running business—they are usually sold as land, as machinery, as cattle. This would attract GST and, if that is correct, then the farmer selling his farm at the end of his life—which I am faced with in another few years—basically is the farmer's interpretation of a superannuation package. The day we sell out is the day we feel, 'Well, we've starved the last 30 years but it is all worth it. We've got a nice lump sum.' If GST applies there I have simply had 10 per cent taken off my superannuation.

So I ask the good senators whether they would be terribly happy with a 10 per cent drop in their salaries and 10 per cent slashed off their superannuation—I am not sure. In saying all of this I think it is public knowledge across Queensland that I have been a coalition supporter publicly for a long time. I think it is also public knowledge that we are probably the only rural organisation who is saying the GST is not going to do us any good. I think that is because we are beef specific and our membership includes everybody from supermarkets to producers and our view is a little bit different. But I can assure you that if I thought the GST was of benefit, and given my political feelings, I think I would be saying so. So I am probably a little bit out of favour with some people who know me, but I feel that that is the truth of the economic impact on a beef producer's business.

**CHAIR**—Thank you, Mr Jeremy. Is it your intention to invite Dr McGovern to supplement your remarks?

**Mr Jeremy**—Yes, it is my intention to invite Dr McGovern to comment. He is an economist and he talks another language to me, so when we get to questions you might have to swap a little because there are things I can answer which he cannot and vice versa.

**CHAIR**—When we get to questions it will be up to you to decide which one of the two of you answers.

**Mr Jeremy**—Thank you very much.

**Dr McGovern**—First of all I think my overall position on the GST is there are more questions than answers. I applaud the efforts of this committee to get some answers. I am looking forward to seeing what you do come up with, because it seems really ridiculous that we have been talking for over 20 years about this tax and we have never had a decent investigation. What we have had are assertions and unfounded statements, and we have got

all sorts of things. The weight of evidence has led me to conclude that the GST and the tax pack—with particularly the GST shift of it—can turn out to be flawed on theoretical, empirical, logical and evaluative grounds.

Just to run through those four headings, there are the theoretical issues. The practical issues Dick has addressed. It is obvious to anyone who has ever been to a saleyard how prices are set. With regard to how we think about it in terms of theoretical issues, before the election I am sure a lot of you have seen this little booklet on the new tax system—

**Senator SHERRY**—Is it part of a set?

**Dr McGovern**—This is part of the information before the election from *Tax Reform: not a new tax, a new tax system*. Turning to the middle of the book there is a diagram, on page 10 of the booklet, which shows the value added chain. It has four producers and they all add on their 10 per cent. I am sure you have seen this sort of thing in the papers. It was all through the press. It says, ‘Here’s an enterprise. It adds on 10 per cent and passes it on.’ Right? Of course, that is a load of rubbish. To simply say that any business in any situation can simply add 10 per cent on and pass it on is a load of rubbish and yet it is public information. Where did the information come from? The foundation for that sort of information—have you seen anything like that before?

We can actually go back a good 20 years to the Asprey report. If you have caught up with the Asprey report I do not need to explain the background to that. At page 518 of the Asprey final report the same table is present with slight variations. This goes to the heart of our thinking. From an administrative point of view it might be lovely to assume that people can pass on things but economically it just does not happen in real world markets. At the core of these claims about businesses’ ability to pass on lay some fairly important economic issues. Those of you who have been lucky enough to do first year economics might have had a textbook something like McTaggart’s book. You turn to a section where they talk about the impact or the incidence of a tax. It is all there. It is in first-year books, it is in second-year books, it is right through the literature that suppliers and demanders share a tax. It depends upon the relative market elasticities and all this sort of thing and I am sure you have heard lots of debates about this from the CGE models.

**Senator CONROY**—Not enough debate.

**Dr McGovern**—Not enough?

**Senator CONROY**—No.

**Dr McGovern**—Okay. We get to the issue of how much do people actually pick up? I will just step aside for a second. Having taught first year economics, this is an area where only the better students get hold of it. Unfortunately some of these better students do not seem to be penetrating public thinking. I will leave that as a challenge because I am going to suggest to you that Australia as a country has been underinformed in its public policy areas and the GST is one very clear manifestation of this. Let us turn to another book, since we have all got past first year occasionally. I have the weight of evidence, if you like, that I am just stacking up here because I am sure there are other things in life. Referring to a book

like this one by Kreps on microeconomic theory—those of you who sat through the arguments about various elasticity levels and general Euclidean models and things like that—I will just give you one quote out of here, and this is with regard to any tax:

When we tax wages or impose excise or sales taxes or any other tax on goods or services, the price at the buyer and seller face are then forced apart and there is no particular reason to think that efficiency will result.

That is the theoretical argument: there is no particular reason to think the theoretical result of efficiency will occur necessarily.

So it is not a question that the market will actually sort it out. We do not expect the market to sort it out necessarily. There is the whole welfare criteria and so on which these sorts of books go through, or other books like this one on welfare economics. The welfare theories that the market will deliver appropriately fall down and, quite fundamental also, the requirements that investments be repaid. All of those of you who think that business is your constituency, it is incredible that a lot of these business people get up and they push models which assume away investment returns. They just assume the investments are going to be there. If the market moves against you, there is nothing in the theory to highlight the fact.

So what I am getting at here is that on theoretical grounds we can actually see some real problems here in terms of the possibilities of the market working. What we come back to in a practical sense is that value judgments are going to be inevitable. The short answer to the whole thing is that it is not a matter of getting the most efficient or anything like that; it is saying, 'Compared to the present situation, will the new situation be more or less efficient?' So I think all these claims of virtuousness should be discounted quite heavily because the economy is not about virtue, it is about practicalities of relativities and buying and selling—all those sorts of things. It is up to the public policy area and the political agenda to actually make some weighted decisions here.

I would suggest there are various biases in a GST. One bias is that it favours exporters over importers. From a balance of payments position that is a very important question. Why differentiate, because an import replacement or an exporter both contribute equally to a balance of payments situation. So why make a virtue of exports and not import replacement? Second, it seems to me from what I have seen—and I welcome further discussion on this—that large businesses are preferred over small. There seems to be an in-built bias for a number of criteria. Thirdly, creative accounting allows avoidance and evasion. In the case of agriculture in particular I think it differentially is negative. I have written a couple of columns on this and I will provide these for further reading.

So we have these effects. I can sum up all that I have said so far by saying that there are structural inefficiencies arising from a GST which I do not think have even been looked at yet. It is fascinating that it seems likely to me that those in more competitive markets are likely to appear to be relatively more disadvantaged. The more competitive you are, the less likely it is you can pass on various costs and taxes. If you have a bit of monopoly power, sure, you have the opportunity, perhaps. So it actually could work against the whole competitive ethos that is supposed to have been driving Australia for the last five or 10 years and could reinforce positions of monopoly. That is something which I think is quite critical in terms of the dynamic development of the Australian economy.

One thing which, in the light of overseas experience, needs some serious thinking about is the possibility the economy might somehow stall as relativities change in ways that are uncertain, and existing investments and plans are reassessed. It is an interesting coincidence that Japan went to a GST and it then stalled, and it is an interesting coincidence that Europe went to a GST in various countries and then went to high unemployment levels. It is also an interesting coincidence that countries like Australia and the US which, as I am sure you know have not had a GST, have outperformed those that have on many measures.

If I could turn now to the empirical modelling undertaking. This is where the numbers are in terms of the beef-specific modelling which has been done by people like the Centre of Agricultural and Resource Economics at Armidale and the Centre for International Economic Modelling—are you aware of their modelling findings from what you have heard so far?

**CHAIR**—I am not aware of them, no.

**Dr McGovern**—Okay. Basically the position as quoted by the National Farmers and various other groups has relied upon two models. One was a whole of farm model, which was the CARE model. It said, ‘Here’s the farm. How will various things change?’ and it included the income tax returns and all this sort of stuff. It was done without allowing for price changes. So it was assumed the prices would stay the same but the farm would adjust. So there is a deficiency there. There was a net gain for the farms model which was relatively slight. I cannot remember the figure but I have got it in the paper there. The interesting finding was that if you just looked at it for about 15 minutes, probably, and played around with a few numbers, a one or two per cent price increase would take away the gain to the beef sector’s model, or the farms model to be more exact. That model I think was only partial, and having talked to the people at CARE they admit it was only partial and there should have been more done.

The Centre for International Economics model basically argued the general equilibrium style: that if you allow all the markets to adjust, and assume the farmers can hang in—and the question Dick was raising was, ‘Can the farmers really hang in any better in this situation or are they much worse off?’—after all the markets adjust, the way Australia is going to be better off is that we are going to export more cattle for a lower price. That, to me, is a perverse finding. That is one which was then picked up, and it was said, ‘Well, that’s the story.’ I can speak further on those two models.

I put this out in an article through *Beef Improvement News* last November, and also at the time *Stateline* in Queensland ran a program. On that there were some people from the National Farmers. One of the comments from Mr Douglas of the National Farmers, when asked were the models rushed—and this is reasonably close to a quote and I have got the tape and if we had a video we could watch that—was, ‘It was always our intention when undertaking the modelling to include the price effects but unfortunately the time between when the tax pack was announced and when the election was called meant there was little opportunity.’

In other words, partial modelling is being used inappropriately. I think this is something that in the time that is remaining there should be more of. Some of it can be really simply done. You just look at the assumptions and say, ‘Okay, they’ve done all this modelling but

what is the overall set of assumptions?’ It is interesting that the response by the National Farmers to my criticism on that program was not to ring me up and say, ‘Hey, we think you’re wrong. Let’s talk about it’ or, ‘You’re a silly twit’ or anything like that, it was to ring the ABC management and complain. So that is the level of public debate in trying to get an understanding which I think deserves a closer look.

The general equilibrium modelling has Dixon and co. and Murphy and all those sort of people—I am sure you are right up on that one. I will just simply remind you that general equilibrium modelling relies upon a series of assumptions which embody their own picture of the structure of the economy. Whether that structure will actually be maintained under the sorts of changes in the tax pack is a very open question. You can only assume so much change in the economy.

**Senator FERGUSON**—Are you saying we should not take too much notice of Dixon and people like that?

**Dr McGovern**—What I am saying is that general equilibrium models give—

**Senator CONROY**—Nice try, Fergy!

**Dr McGovern**—an interesting set of answers which you then need to properly evaluate in a wider setting. The questions that you might raise on those are the balance of payments effects coming out of those—they are likely to be reasonable sort of estimates—and things like the profitability, and I have not seen any estimates of those sorts of things. I think in terms of relative prices changes, that is what they should probably model best. I certainly would agree with the comments made there that things like the CPI are an inadequate basis for measuring household consumption or anything like that. I think the household expenditure survey is a reasonable thing.

**CHAIR**—Is it a reasonable thing to model what we have called the pass-through assumption, that is, whether or not the reductions in prices due to cuts in wholesale sales tax will be passed on immediately—and one of the things that we did want to model in the work we commissioned with Dixon was whether or not there is a 100 per cent pass through—and what would be the effect on the economy if there were, say, a 70 per cent pass through, things like that? Is that a reasonable approach—to look at a range of assumptions rather than one given assumption?

**Dr McGovern**—Yes, sure.

**CHAIR**—Treasury has based theirs on the assumption that it is immediate and it is 100 per cent. We looked at a range of other assumptions.

**Dr McGovern**—I think I would just go back to the first year textbook and ask Treasury to please explain, and say, ‘The incidence of a tax is usually shared.’ I mean, it is as simple as that. The only place where you will get a perfect passing on is where there can be no consumer response, and that is not even in a monopoly case, that is an ideal of—well, I do not know what you would call it.

**Senator CONROY**—That is your market stall, isn't it, in the first year—down at the market?

**Dr McGovern**—Yes, it is a weird situation. I think, looking at the practical situation, just going back to the models, in terms of time framing, the general equilibrium models cannot actually build a time frame in the way they are structured. All they can do is say, 'After all the effects have happened, this is our final state.' If I can put it another way, all the modelling is based upon the idea of, 'Here is our initial state. We will traject ourselves to a final state,' and it is comparatively static. What we have not got is any cosmogony. We have no theory of how the world develops, and so the sorts of things that Dick was saying about the practicalities, the cosmogony of how business is actually carried out, are missed by the model.

On the other hand, if you listen to businesses all the time you miss the possibility of these big pictures. So this is where you have got the very interesting challenge of actually trying to work out where the truth, so to speak, lies. But you will never find a perfect truth. All you can say is, 'This seems to us, on these good grounds, a marked improvement.' That is I think as far as we could expect you to go.

Let me just also go to something really simple that you can pick up from something like the national accounts. One of the claims that has been made is that the rural sector will be better off because of transport savings and things like this. So if we turn to the national accounts to, say, table 2 where there are lots of nice numbers, but basically if we take the beef sector in particular, which is 0103 as a sector, Australian production is \$4 billion, roughly. The transport component of that is about \$140 million. If we look at that other value added, the operating surplus, it is about \$1.7 billion. If that is the part that is going to be hit by the GST, 10 per cent of \$1.7 billion is \$170 million.

What we would need to do to compensate through transport is to get transport for free. That is the order of magnitude change you have got to have. Transport operators cannot be got for free. So I think for those sorts of things you say the order of magnitude does not look right, and I think this is the sort of roundabout discussion which can be done quite quickly and which I think can give you an idea of the sensitivity to change. That is the only way I think you can come to the question of Dixon's models or any other sort of models—I do not think they can be discounted, but they need to be interpreted in a way that is reasonably informed.

If I can just digress quickly on this one, a couple of years ago the Department of Housing and Regional Development got me and a couple of other people to evaluate the various general equilibrium models so we held a couple of days in Canberra and all this sort of thing. One of the first questions I asked DHARD was, 'What do you want the model for?' and they did not know the answer. So my question back to you is, 'What are you wanting to get out of the model? Have you got some specific things?' Then I can tell you whether the model is adequate or whether it should be discounted.

**CHAIR**—The specific things are set down in our terms of reference. In our first report we had to come to grips with what the macro-economic implications of the tax would be, the impact on growth, employment, inflation, export competitiveness, a range of issues like that.

**Dr McGovern**—Okay, so in terms of those questions, yes, you have probably got as good a model as you are going to get at that macro level. What is missing, though, are the micro foundations of how does it impact on business activity and profitability? In other words, how does it really impact on the economy? So we have got our trajectory but we do not really know what is going to happen, and we can only be guided by things like elasticities and all that sort of stuff.

I had better quickly move on to the two final points, which will not take as long. The question of flawed logic: the assertion that the GST or taxes like it are taxing goods or services I would disagree with. They are actually a tax, as far as I can see, on the value added by the providers of the good or service. So it is not imports, say, that are taxed, it is the importer's margin that gets the tax. So we are actually taxing the margins of businesses.

How does a business offset this? This is getting to, as I say, the micro response. It may be passed on to consumers, but if consumers are budget constrained or if there are situations in the market of competition, especially if it is perfectly competitive, then they cannot pass it on, especially if it is also an open economy. Then they try and pass on their cost to labour, squeeze returns, or they may actually reduce labour and that could explain the European high unemployment for a number of years. They may try and pass it on through productivity gains but, given the substantial increases in productivity in Australia over the last few years, we wonder how much room there is for this sort of thing, but there might be something. They might try to pass it on by selective international arrangements of production and consumption. In other words, you organise your affairs to fit the tax system, not because of comparative advantage or competitive advantage or anything else, but simply because of financial arrangements—and that leads to a major misallocation of resources.

The final comment is on the basis of evaluation. I would suggest, from the little bit I have read of a couple of things, that it seems the basis of evaluation is being stated as efficiency and equity and simplicity. Here again you are following Asprey. It is my recollection from economics that it is a little bit more than simplicity. There basically is something like enforceability. There is no point in having a tax unless it actually can be collected. I think the use of the idea of simplicity is a very poor approach, especially when you start to say uniformity then becomes part of the whole game. If you say the tax is uniform in its application—which has been said many times—you are discounting economic theory. It might be, from an accounting point of view, but it is not economics.

I was talking to Professor Ted Kolsen—who we had hoped would come along today but, unfortunately, he was tied up as his wife has been ill—and one of the things Ted said was that when Asprey came out, the economists did not get into it too much. It was seen to be left to the lawyers and accountants. So that is something which I think we, as economists, probably owe an apology to the wider public about, because I do not think it has been properly looked at.

**CHAIR**—I am sorry, Dr McGovern, but I must ask you if you are close to your conclusion.

**Dr McGovern**—Yes. There is one comment Ted made which I think reinforces the final point. Ted's comment on the theory and the practice was that a tax where 'a Barbie doll's

price falls from \$20 to \$18.55, while bread rises from \$1.95 to \$2.13 may appeal to some, but not to me.’ At the end of the day that is the sort of question that is fundamental in all this: the distributional issues. If we then take it to beef producers and others in rural Australia, I have a number of grounds which I have suggested to you will mean that people in rural Australia will be markedly worse off from the tax pack. The modelling that has been done so far has been partial and it has shown slight gain or slight loss; it has been shown to be very close. I think if we take it a bit further we can find some major areas of potential loss.

**Senator CONROY**—Some would say selective.

**Dr McGovern**—That is their opinion. What I think we have been lacking is any proper dialogue—a robust dialogue—on those sorts of models so far. Thank you for your time.

**CHAIR**—Thank you both. You have raised some objections to this tax so let me ask the standard question I ask most witnesses: are you asking the Senate to amend the package to reflect the views that you have put?

**Mr Jeremy**—To amend the package?

**CHAIR**—To amend the package of bills. There are 16 bills we will have to vote on, I am told, before 1 July.

**Mr Jeremy**—I am sorry for you.

**CHAIR**—But we have to make a decision about it and we are collecting information. Is the Beef Producers Association saying to us, as representatives of the Senate at this inquiry, that you would like us to amend the bills to reflect the concerns you have put to us today?

**Mr Jeremy**—I would prefer you to vote against them.

**CHAIR**—You prefer to vote the lot out?

**Mr Jeremy**—Yes.

**CHAIR**—Okay. The other question I have is really from an export point of view. A major market for meat exports is North Asia. The economy of Japan is in recession and the economy of the Republic of Korea was in deep recession but is just coming out of it now with IMF assistance. What have the economic difficulties of those two prime markets done to demand for your product?

**Mr Jeremy**—The demand is basically there at ground level. It is just that we live in a country with rising costs all the way and we are now getting 1984 or 1985 prices for our product which is making our industry unviable. There is no prospect of that rising.

**CHAIR**—This is because of world supply outstripping world demand?

**Mr Jeremy**—That is right, yes. We are basically in an overproduction phase around the world because everyone assumed, on models, that the Asian market countries would continue to rise in prosperity and move with us, but this has not happened.

**CHAIR**—This is typical of most agricultural commodities, as well as mineral commodities, I must say.

**Mr Jeremy**—I think it would be, yes. You are right, because we live in an economy where everybody expects more every year and there are plenty of other places in the world that are on a very level economic movement, I think.

**CHAIR**—My point is, just to re-emphasise the point you made earlier, that we are price takers not price setters.

**Mr Jeremy**—Price takers, yes.

**CHAIR**—And that is not typical just of beef but of a whole range of agricultural commodities we export and the major mineral exports as well. That is probably an unfair question for you, Mr Jeremy, because it is outside your field of competence.

**Mr Jeremy**—I did make the point earlier that we are beef specific.

**CHAIR**—Yes.

**Mr Jeremy**—Whereas many of the rural groups you have been getting advice from probably cover more than one commodity.

**CHAIR**—Indeed.

**Mr Jeremy**—I can imagine that, say, in the case of wool, really the producer owns the wool until it hits the wharf and his buyer is actually somebody in Japan or China, so the GST problem does not arise the way it does with the traded, manufactured product or animal that goes through three or four hands.

**Senator FERGUSON**—That is not necessarily true. There is a lot of wool sold to private growers.

**Mr Jeremy**—As I say, it is outside my level of expertise and I could not say that it is bad for every farmer, but I can say clearly that it is not going to help the beef industry.

**CHAIR**—In relation to the question of the trend line, in terms of your international market, I saw some figures published in the *Financial Review* yesterday which showed demand for agricultural commodities and the price cuts that have had to be absorbed. What is the outlook for your industry? Will you return to higher prices, or is the outlook more of the same, or is the outlook that you will get worse?

**Mr Jeremy**—The outlook generally for beef is that we should see some rises over the next couple of years, but very slight. This is mainly because of the American herd situation.

Their output is declining and that will interfere with our export markets to a lesser degree than it has. When they are in hard production they push beef onto our export markets. Their production is now declining so we have a chance to move our export prices up a little bit, possibly, over the next couple of years, providing Asia holds together in reasonable shape.

**CHAIR**—That small increase does not suggest nirvana for the beef industry; that just suggests slight relief on the toilsome problems you have now, doesn't it?

**Mr Jeremy**—That is right. We may get back to surviving instead of declining seriously on a financial base.

**CHAIR**—Is your concern that the GST will sop up those gains and just leave you where you are?

**Mr Jeremy**—Exactly.

**Senator FERGUSON**—I have listened carefully to what you have said, Mr Jeremy, and also Dr McGovern, who talked a lot about first year economics. It reminded me of the story about the person who was asked where he spent the best three years of his life and he said, 'Doing first year economics.' I have not done first year economics but I know Senator Conroy has, so we should be all right. I have more in common with you, Mr Jeremy, because I have been a primary producer for most of my life and have been a price taker, not a price setter. But you do have some misconceptions about the current system and I think we ought to allay some of your fears, which may make you change your attitude to some of the issues you have raised. Why wouldn't someone pay \$11,000 for your stud bull that currently he would pay \$10,000 for, knowing that he would get the \$1,000 back as a GST credit?

**Mr Jeremy**—Because he does not get that back until he resells it, or turns it into beef, or something.

**Senator FERGUSON**—No, I am sorry; he gets it back immediately. He gets it back as soon as he puts his return in, because it is an input cost which is rebatable to him at his next quarterly return. If he bought it on 20 March, it would be returned to him within four weeks. So why would he not pay \$11,000, knowing he is going to get it back straightaway?

**Mr Jeremy**—I think you would have a market equation there where these things are relative in the buyer's mind; if the abattoir animals come back by buyer percentage, then people expect the whole general scene to come back by a percentage—

**Senator FERGUSON**—But why would the abattoirs come back? You quoted the case for \$300 beef bought by a company that has an export contract. In fact, if they pay \$330 they will get the \$30 refund because there is no GST on exports.

**Mr Jeremy**—As I understand it, when the beast goes export they do not have to pass that component back.

**Senator FERGUSON**—I am sorry; what they do is put in a reform. They do not charge GST when they sell it, but they get back the GST that they have paid on that beast, so in fact the beast still only costs them \$300.

**Mr Jeremy**—But, as I understand it, if the beast goes domestic they have to pass the 10 per cent back down the chain.

**Senator FERGUSON**—No, they still could claim their GST cost and it goes on to the final consumer.

**Mr Jeremy**—If it goes export, as I understood it, it does not have to be passed back.

**Senator FERGUSON**—I am sorry. You do not understand it, Mr Jeremy. If the beast is exported, in fact the GST that is paid is refunded and forwarded to the exporter because there is no GST on exports. So they are two of the issues that you raised.

**CHAIR**—You are not an exporter directly, are you, Mr Jeremy?

**Mr Jeremy**—I am not a direct exporter, no.

**Senator FERGUSON**—It does not matter. Whoever buys it will get the GST.

**CHAIR**—He is not the exporter though.

**Senator FERGUSON**—But the refund will be paid to whoever pays the GST on the price of his animals. So in fact the net cost to the person that purchases is no greater than it is today.

**Mr Jeremy**—I am quite amazed. If our accountancy firm—who did a workshop on GST last Friday—advised me that, I would find it hard to believe that they were wrong.

**Senator FERGUSON**—I promise you they are.

**Mr Jeremy**—With all due respect, if you are right, you are right, but—

**Senator FERGUSON**—I would like to know the name of your accountancy firm, because we would like to put them right. If you could let us know who the accountancy firm are we will make sure the right information gets to them so that they are not misleading people that they are giving advice to. In relation to the sale of a going concern, your farm, you are concerned about losing 10 per cent of your superannuation. You will not, because in fact if your farm is sold as a property and it is still going to be used for farming purposes, there is no GST on the sale of land, so in fact your superannuation will not be touched, if that is what you say your superannuation is. So again you have been poorly advised.

Can I also ask you a question in relation to transport costs. You talked about the New South Wales road transport or a group of transport people—

**Mr Jeremy**—livestock association.

**Senator FERGUSON**—who said that they are having a dreadful time now; their profit margins are so low that in fact they would keep some of their costs in relation to the GST. Why don't they put their prices up today so that they are not in such a difficult position?

**Mr Jeremy**—Because of the enormous competition within the game, isn't it? They are extremely competitive.

**Senator FERGUSON**—I understand. Why won't they be just as competitive after a GST is introduced? Are you saying competition is going to suddenly disappear because we introduced GST and diesel fuel rebates and all of those sorts of things?

**Mr Jeremy**—The competition will still be there. They are certainly seeing it as a possible help with their problems.

**Senator FERGUSON**—But it is no different today. They could put their prices up today if they wanted to, if they thought they could get away with it. They know they cannot. After the GST is introduced and there is a saving in diesel fuel, exactly the same situation will be invoked tomorrow as it is today, the day after GST is introduced as the day before. Competition is what will make them keep their prices down; otherwise they would put their prices up today. Can I suggest a couple of other questions. How many members of the—

**Senator SHERRY**—You can answer the question, unless there is a barrage or a lecture, and you can—

**Senator FERGUSON**—Sorry, Senator Sherry. Senator Cook is in the chair.

**Senator SHERRY**—So what?

**Senator FERGUSON**—Well, you are not.

**Senator SHERRY**—So what?

**Senator FERGUSON**—Are you going to run the show? Senator Cook, Senator Sherry would like to be the chairman.

**CHAIR**—Order! The committee will come to order.

**Senator SHERRY**—I want to see a witness get a fair go—

**CHAIR**—The committee will come to order.

**Senator SHERRY**—rather than get a lecture from you—

**CHAIR**—Order!

**Senator SHERRY**—and an opportunity to answer some questions.

**CHAIR**—Just hang on. Everyone: just take a deep breath, will you. I would rather members of the committee did not pick on one another or make snide remarks to one another but simply directed their questions to the witnesses.

**Senator FERGUSON**—Well, I did not say anything, Mr Chairman. I was interrupted.

**CHAIR**—Order! I am addressing the committee. If that is understood, let us proceed.

**Senator FERGUSON**—How many members are there of the beef producers association?

**Mr Jeremy**—We have got about 1,400 around Australia.

**Senator FERGUSON**—How many members are there of the Cattle Council of Australia, do you know?

**Mr Jeremy**—There are 24 or 25 members.

**Senator FERGUSON**—Sorry. I understand it is a member organisation.

**Mr Jeremy**—Yes, it is a member organisation. It is the representative of state bodies.

**Senator FERGUSON**—How many people does the Cattle Council represent?

**Mr Jeremy**—They would represent probably 2,000 or 3,000 people per state possibly.

**Senator FERGUSON**—That would mean something like 12,000 or 15,000 possibly all round.

**Mr Jeremy**—That would be maximum, yes.

**Senator FERGUSON**—Why do you think it is that they have a different position in relation to tax reform to your own body?

**Mr Jeremy**—Because the state bodies are multicommodity bodies.

**Senator FERGUSON**—What, the Cattle Council?

**Mr Jeremy**—No, the state bodies that drive the Cattle Council are multicommodity bodies, and having paid the piper you call the tune. It is quite simple. So you have a state organisation which may have controlling interests—by wool or wheat or any other various commodity—and they have links with the NFF, and the Cattle Council is in the position of being appointed people who draw a salary and they are not as sensitive to members' wishes as we are.

**Senator FERGUSON**—So for this submission that you have put in here, you have gone around and seen all of your members and collected their views?

**Mr Jeremy**—Not everyone individually, no. But we run surveys.

**Senator FERGUSON**—Just one final question to Dr McGovern. It is obvious that when you talk about the price of a Barbie doll and the price of a loaf of bread, which your professor—I forget his name—alluded to, in fact as far as I can see, he is the only person who believes that a loaf of bread will go up by 10 per cent. Every other economic model and every other advice and all the other evidence that we have actually had before this committee suggests that the maximum price of an increase in a loaf of bread is about 5.8 per cent. So I am wondering why you quoted 10 per cent. Is he the only one that thinks that?

**Dr McGovern**—I have got several points I would like to make at this stage. Firstly, I think the senator, with due respect, does not understand the way a market operates.

**Senator FERGUSON**—I have been involved in it for 40 years.

**Dr McGovern**—If we go straight to the end of the point here: if the price only goes up by five per cent or so, that means that various tax increases along the way will be absorbed somewhere. This will have an impact on profitability. The key thing I was trying to get through at one stage was that there has been no assessment on profitability for various sorts of enterprises. It would appear to me that agriculture is likely to be less profitable and this would be consistent with the CARE model bill, the compensation coming through social security, so the total impact of the tax pack is to move us from profitable business to social security. That is in the CARE model, and I suggest you look very carefully at it. The net effect is slightly positive if the income tax effects and all that sort of thing are there.

If you want to keep inflation below 10 per cent or some other figure, you have got to ask yourself the question, ‘How are these various costs going to be actually absorbed?’ and this is where I go back to the simplistic accounting thinking which bedevils the whole debate. It looks superficially very attractive because this idea that people can actually somehow pass on 10 per cent willy-nilly, as I tried to indicate before, is very difficult in competitive markets, and that is what you were agreeing with. If transport operators are going to absorb the tax somehow, then there has got to be offsetting changes for them and they may be there. But it is interesting that the RACQ, for example, which should know motoring and transport, calls it dynamite and basically says motorists will end up paying more.

**Senator FERGUSON**—Has that got anything to do with transport operators?

**Dr McGovern**—In terms of the things they particularly picked upon—and there may be some areas which need clarification here, which is one of the reasons why I was bringing it up—things like repair costs that they expect to rise.

**CHAIR**—That is consistent with what the RAA in South Australia told us.

**Senator FERGUSON**—I accept that.

**Dr McGovern**—The thing that I am disappointed in is that Senator Ferguson adopts a tone which is, to me, saying, ‘This is the story and this is the political game being played,’ rather than saying, ‘Well, why aren’t we getting to the basis of what’s really going on in our

economy?’ and this is the challenge which I think is ahead of this committee, and not necessarily today or tomorrow. If I can turn to one issue which I think sums up the whole misunderstanding: the beef sector obtains about 40 per cent of its income from the domestic market and 60 per cent from overseas. The domestic market is likely to be affected differentially for something like beef compared to other foods. The effects on bread are probably going to be small, and the effects on beef will probably be greater. So there is a differential effect which prejudices beef producers compared to, say, flour makers or growers. They are the sorts of shifts. If you wish to do that sort of thing, that is fair enough. That is your decision. But be conscious that they are the things you are doing. You are picking some winners. De facto you must pick some winners in this game.

**Senator FERGUSON**—Did you read the results in here of the cost effects by industry of indirect tax reform as proposed by the government, where in fact the cost effect on the beef cattle industry is that they will have a cost reduction of 2.8 per cent?

**Dr McGovern**—This is in which model, please?

**Senator FERGUSON**—In that tax reform booklet.

**Senator SHERRY**—The price effect is a 6.6 per cent increase.

**Senator FERGUSON**—No.

**Senator SHERRY**—Price effect.

**Senator FERGUSON**—Sorry, I am—

**Senator SHERRY**—Price effect on meat products.

**CHAIR**—You can have your—

**Senator SHERRY**—Meat and meat products. I thought you had just finished.

**Senator FERGUSON**—No.

**Dr McGovern**—Okay. Well, I have not seen the report. I will be happy to—

**Senator FERGUSON**—It is not a report; it is actually the whole document. It is the tax reform.

**Dr McGovern**—Okay, I would be happy to provide further discussion on that. I have not seen that full one. I could not get it off the Internet at the time, and I asked for it to be sent and it was not.

**Senator FERGUSON**—This was available prior to the election.

**Dr McGovern**—I will repeat my statement for clarity. I asked for it to be sent. It was not sent. I could not get it off the Internet because it was not printing properly. So all I

could do is show you the booklet which I have got here. Could I ask who the modeller was, please? Who did it?

**Senator CONROY**—There isn't one.

**CHAIR**—Order!

**Dr McGovern**—Could we have an attribution of who is the modeller and the model they have used, please?

**Senator FERGUSON**—The individual person you want to know?

**Dr McGovern**—No, I would like the department or the person that modelled it.

**Senator FERGUSON**—The PRISMOD model.

**Dr McGovern**—PRISMOD? And who would be the contact person?

**CHAIR**—Well, it is the Treasury model.

**Dr McGovern**—The Treasury model?

**Senator CONROY**—Ken Henry is his name.

**Dr McGovern**—Okay.

**CHAIR**—Senator O'Chee.

**Senator O'CHEE**—Thank you, Mr Chairman. I will attempt to be brief. Paragraph 1 of your submission says:

Anecdotal experience in New Zealand points to a 10 to 15% fall in beef consumption following the introduction of their GST.

Where do you derive that information?

**Dr McGovern**—I am not sure of the source of that. That needs to be attributed.

**Mr Jeremy**—That is anecdotal evidence from New Zealand.

**Senator O'CHEE**—Would you be interested to know that the meat and wool economic service of New Zealand today sent a fax to the Parliamentary Library advising that in 1986-87, the year in which GST was introduced, the kilo per capita annual consumption of beef rose from 34.59 kilos to 36.23 kilos per capita. It actually rose in the year in which GST was introduced, and it rose in the subsequent year. That does not seem to bear out your assertion, does it?

**Dr McGovern**—Could you tell us what the price effects were in those two years and the profitability effects?

**Senator O'CHEE**—You are saying that it will fall 10 to 15 per cent. I am saying it is not borne out by fact.

**Dr McGovern**—Two things: one is, I did not prepare this statement so I cannot speak to the statement without knowing where it came from. Secondly, to assess it properly you need to know quantity, price, and profitability effects.

**Senator O'CHEE**—Yes, but we are just going through your submission.

**Dr McGovern**—Yes, okay, the submission needs then to be modified.

**CHAIR**—Can you conclude your questions, Senator O'Chee.

**Senator O'CHEE**—In one go, Mr Chairman?

**CHAIR**—I am policing the question time, clearly, and the coalition has had over 20 minutes so far.

**Senator O'CHEE**—Okay, I will see if I can roll this into one question. You say at point 2 that there is no income tax reduction to offset the increase in costs. But all business inputs are rebated in full, as I think Mr Jeremy now understands. You also say that the separation of paperwork for tax exempt beef from tax domestic beef from the same carcass appears to be an administrative nightmare, to which I ask: do you understand that it is calculated on total purchase costs and total sale prices, and therefore you do not need to separate out individual cuts from the same carcass?

Finally, you assert that the package favours exports over import replacement, in which case you might like to turn your mind to the fact that overseas exports from New Zealand to Australia, for example, of red meats currently do not attract any indirect tax, and all their input costs are tax rebated in full. So surely what it does is in fact support Australian replacement of imports from overseas by eliminating the artificial tax constraints currently carried by the Australian product. You can take that on notice, if you like.

**Dr McGovern**—Yes. On the last one, would you just explain again, please: import replacement for an Australian business replacing an import from, say, New Zealand?

**Senator O'CHEE**—Mr Jeremy asserted that the package favoured exports over import replacement, but New Zealand exporters who send product here have all the tax on their inputs rebated in full, whereas the Australian product sold domestically without this tax reform package has none of the input costs rebated.

**Dr McGovern**—But aren't I correct in saying there is no sales tax paid on primary production at the moment?

**Senator O'CHEE**—But if you have lots of indirect costs built into the whole process and if this is—

**Dr McGovern**—And these would be things like transport costs and taxes?

**Senator O'CHEE**—Transport costs and costs in the meatworks and handling and retailing.

**Dr McGovern**—Yes, and the margins there I estimate—I mean, I gave you the example of transport, \$170 million and \$4 billion.

**Senator O'CHEE**—But you have to admit that this package eliminates some of the discrepancies currently favouring New Zealanders which exist at the moment.

**Dr McGovern**—Indeed not. No, that to me is not at all clearly established. What I think is clear is that, if you are an exporter selling into an Australian market, you are under a different tax regime to an Australian selling in an Australian market and, depending upon where you are in the economy, you may be better off but you may well be worse off, because what you are doing is saying that, if you sell locally, you cannot reduce your prices—sorry, you cannot get rid of the GST—if you export it overseas. So, if we take a two-country model, we export to them and they export to us, and basically both run each other down because the domestic market cannot avoid the 10 per cent, the GST. All these other margin things may be there. That is one of the things about primary production. I think, off the top of my head, commodity taxes and things are about half a billion dollars.

**Senator O'CHEE**—But their imports, when they are sold in Australia, attract the same rate of GST.

**CHAIR**—Will you finish off, Senator.

**Dr McGovern**—They are attracted on the margin of the import agents, not on the full—

**Senator O'CHEE**—No, on the retail price. New Zealand meat sold in a store attracts the same 10 per cent GST on retail price as Australian meat.

**Dr McGovern**—But can the importing agent not deduct the cost of the imported meat? Or have you got a 10 per cent tariff on meat?

**Senator O'CHEE**—No, what we are talking about is if the—

**CHAIR**—Order! Senator Bartlett.

**Senator O'CHEE**—Well, I am just trying to answer the question.

**CHAIR**—If you do not mind, about four or five minutes ago I asked you to wind up.

**Senator O'CHEE**—Fine, Mr Chairman.

**Senator BARTLETT**—Thank you. In terms of what seems to be one of your main concerns at point 1 of your submission about the impact on the beef industry of an increase in price, if food was zero rated, and assuming meat fell within that definition of essential food, then the price would presumably either stay the same or fall slightly. Would that address your concerns in relation to the impact on the industry?

**Mr Jeremy**—If it was zero rated?

**Dr McGovern**—In terms of foods being exempt, it is probably not going to have demand effects, which would be a positive. It depends on the particular composition of purchasers that are coming into the business store, because am I correct in saying that if it is zero rated you cannot deduct any taxes on inputs? If you are a food producer and you have got a zero rated commodity, can you deduct the costs of GST paid on other things?

**Senator BARTLETT**—Yes, I think so.

**Dr McGovern**—You can? Okay, in which case that may well solve a number of these problems.

**Senator BARTLETT**—Okay, thanks. In terms of your concern about the impact of the decline in beef consumption, if there was this price rise, what sorts of food would people buy instead of beef in that case? Do you think the public would spend less money on food overall or would they switch to other things?

**Dr McGovern**—If there is a real budget constraint they have to cut food, because they have only got so many dollars to spend. Two other things happen: people trade down and go from steak to sausages and those sorts of things, or they go to substitutes. How it would work really depends on all sorts of cross-elasticities. What you would expect, simply put, would be lesser quality beef being favoured, compared to the better cuts in some areas, and movement away from beef, which is regarded more as a luxury compared to some other things like bread. So beef would be hit harder than breads.

**Senator BARTLETT**—What sort of consultation has the NFF had with you or vice versa in relation to the tax package issue?

**Mr Jeremy**—Not very much at all. We tend to find the NFF are in a bit of an ivory tower compared to ordinary people. They look in computers for their models and we look at the chequebooks for our models. It is a different thing. That is why I think a lot of the assumptions in this are made by very dedicated people with very honest opinions, but I am sure that the marketplace is a different field to compare the model; I am quite certain of that. Really, if marketing was a static science and all models ran true, we would have solved all the market and tax problems 50 years ago. All that happens is when you change your tax, or change the rules, or change the regulations, the people simply move around it. They change their way of doing business. It is human nature you are combating. That is why we have laws around the place.

**Senator BARTLETT**—Just at the end of your submission, in terms of addressing some of the concerns you have raised you state that you would like the government to investigate pro rata payments to offset your suggested losses. What do you mean by pro rata payments?

**Mr Jeremy**—That is not really defined. Obviously, if the compliance costs are a serious thing, if the transport costs do not come through, at some further time down the track we would expect that the beef industry will be coming back and talking about compensation somewhere down the line, whereas other farmers may be quite happy with it.

**Senator BARTLETT**—I just want to ask a few statistical questions, all of which you may want to take on notice, about the beef industry. I would be interested in figures, from your perspective anyway, on the percentage of beef that is produced in Australia that is also sold in Australia, as opposed to exported.

**Mr Jeremy**—Forty per cent domestic to about 60 per cent exported in round figures.

**Senator BARTLETT**—And do you have any figures on the levels of beef consumed by various income groups within the community? Is there any research available on that?

**Mr Jeremy**—No, I do not have that. Sorry.

**Senator BARTLETT**—Also, that figure raised earlier, the 10 to 15 per cent fall in beef consumption: the source for that and whether that was immediate or over time.

**Mr Jeremy**—We can certainly get that to you because that figure was produced by the chairman, not by me.

**Senator BARTLETT**—Right.

**Mr Jeremy**—I run the business of ABA but the chairman actually had a lot to do with the actual submission itself.

**Senator BARTLETT**—Sure. Also particularly whether that is over a period of time rather than in the first year or two, as well as issues about the price impact, the price changes, as well—if you did have that, that would be handy. Thank you.

**CHAIR**—We had a discussion—and I use that word advisedly—earlier about what in fact is the impact on farmers. My understanding is—and I think this is in fact the case—that currently you buy inputs to production, purchase veterinary services, put fences in, do all those things which are basically wholesale sales tax free for you.

**Mr Jeremy**—This is true.

**CHAIR**—You will now have to pay a 10 per cent GST on them and claim back at some later time that cost.

**Mr Jeremy**—Yes.

**CHAIR**—You are not an exporter. You sell to a company and that company is the meat company and it exports or sells domestically.

**Mr Jeremy**—Yes.

**CHAIR**—You do not know when a beast leaves your farm on the hoof whether it is going to be an export beef or whether it is going to be domestically consumed, do you?

**Mr Jeremy**—We can make assumptions on the type of animal but there is no way that is accurate. That can be changed down the line at the time; whether the next owner holds it for longer or not.

**CHAIR**—And if you are breeding Kobe beef, for example, it is quite clear that you are going to sell that in Japan.

**Mr Jeremy**—That is right.

**CHAIR**—Yes. But because you are not the exporter, you are not zero rated.

**Mr Jeremy**—No.

**CHAIR**—When you sell your beef you then charge the person who buys it the GST.

**Mr Jeremy**—That is what will happen, yes.

**CHAIR**—That will happen. In the meanwhile you have to carry the costs of administering this tax system yourself. That is where the extra cost to you comes in.

**Mr Jeremy**—That is right. It is the fact we have to lay out 10 per cent on our inputs, which is a cash flow problem; the fact that we have to carry the compliance costs, accountancy costs and things like that and then wait until some way down the track before it gets passed back to us.

**CHAIR**—For any diesel fuel you purchase you have to apply for the rebate after you have purchased it.

**Mr Jeremy**—I understand that is to be the system.

**CHAIR**—I think that perhaps establishes the proper chain. I was not sure that the proper chain of responsibility had been established in our earlier questions.

**Senator FERGUSON**—Mr Chairman, the other link to the chain, of course, is that if you happen to sell cattle you will collect the GST on that sale and the money you collect by way of GST will be yours until you do the next return, so it counterbalances. You collect the GST from the purchaser, you pay GST on your inputs, so in fact you may actually be holding more in GST than you have paid out.

**CHAIR**—That is an arguable proposition. The sequence I do not dispute, but I dispute the conclusion as to whether you may be holding more GST than you pay out.

**Senator FERGUSON**—We have done it for our own farms. They do not work.

**Mr Jeremy**—I do not think there has ever been a case in history where the primary producer came out of any new deal doing any good, and that is the bottom line of this whole thing. Although all you gentlemen would have the very best intentions and work very hard and put up with a difficult life and all those things, I seriously question that the system of laws, bureaucracy and handing down, and all the things that happen after you have finished with it, will ever work one cent in our favour. It never has. I cannot believe that it is going to start.

**CHAIR**—An old retired bloke in Kalgoorlie said to us last week that you would have to believe in the tooth fairy if you believed it would. Maybe you and he agree—I do not know, Mr Jeremy.

The other thing about beef consumption in Australia as a share of the Australian food intake: there is an argument from the Australian Heart Foundation and others that it is better to eat white meats than red meats. Is your share of the Australian food intake as a beef producer declining?

**Mr Jeremy**—It is declining slightly, yes.

**CHAIR**—I do not know what the trends are but, if that decline were to continue, the 40 to 60 per cent split might become 70 to 30 or something.

**Mr Jeremy**—It could do.

**CHAIR**—The domestic market is a surer market for you than the international market. As you have repeatedly reminded us, and rightly, it is overhung by supply. The extra costs that your members have to find to carry through the charges on the GST are going to be taking place in a more difficult or oblique economic outlook for them. Is that not the case?

**Mr Jeremy**—Yes, that is correct.

**Senator CONROY**—Let us go to point 1. I appreciate you said you were not responsible for putting it together but it talks about the Canberra Centre for International Economics.

**Mr Jeremy**—Yes.

**Senator CONROY**—And its model shows a 8.9 per cent rise in the price of beef at retail level.

**Mr Jeremy**—Yes.

**Senator CONROY**—And their forecast of a consequential 0.4 per cent decline in consumption does not fit traditional price elasticity equations for beef. Have you been able to ascertain what will be the outcome with a more traditional price elasticity with that price rise?

**Dr McGovern**—If you have got elasticity runs between about 0.5 per cent for meat to about one per cent for beef, depending on how broadly you define the commodity and depending on day-to-day elasticities, relative to everything else they are probably still reasonably reliable. If you have an elasticity of one, then it is easy if the price goes up 10 per cent, if the quantity drops 10 per cent, and that is the overall effect on the market. So with beef, especially once again your better cuts, which tend to be focused on the domestic market, you could expect that sort of quantity response.

Another way to think of it is that people consume on a budget. They go in and they say ‘Well, \$10 for beef.’ So that is the sort of response we get and that is why the quantity effects on something like beef will vary in effect from something like bread which has got an elasticity of about 0.15 or something like that. This is why supermarkets play games with bread prices. They know people are not going to eat a whole lot more bread, but if they drop their prices effectively on beef they would eat a whole lot more beef. So you have got that sort of elasticity number that would indicate those sorts of effects.

**Senator BARTLETT**—So what elasticity would they have had to plug into their model to come up with 0.4 per cent of their claim? That is almost a positive point, isn't it?

**Dr McGovern**—0.4 per cent. That is pretty highly inelastic. I could work it out for you. I have not, but we could have a go at that.

**Senator BARTLETT**—Have you spoken to them about this elasticity, about what prompted them to put this one in?

**Dr McGovern**—I have not actually spoken to the Centre for International Economics on this model. My comments on their article were that basically the various estimates around were inconsistent and I did not have time to take it further.

**Senator SHERRY**—The best case scenario you face on the elasticity of demand is a decline in consumption of 0.4 per cent, but you suspect it will be a more significant decline.

**Dr McGovern**—I expect so, on normal market behaviour, yes. What you require for the effect to be that small would be sufficient income gains across the economy; in other words the compensation would be high enough so that the income effect would swamp the elasticity problem. I am not sure that is there in the way that the present package is at all. I would expect that if the prices coming through are up eight per cent or so, then you are going to get a marked drop in beef.

**Senator SHERRY**—The government's ants package: if we look at the price effect of the GST and replacement of some indirect taxes, the price of meat and meat products will go up by 6.6 per cent. Does that reinforce your view that there will be a decline in meat and meat product consumption?

**Dr McGovern**—Certainly. The elasticity I saw in the Orani model was about 0.5 per cent, I think they were using, so you would get a three per cent drop in quantity, roughly.

**Senator SHERRY**—You said a 60-40 split, 40 per cent of meat sold domestically. What is the total value of that market, the 40 per cent that is sold domestically?

**Dr McGovern**—A couple of billion, 1.1 something billion. I think it is about a \$4 billion industry. You have got to take it at the meat manufacturing stage. This one has got meat and dairy together. I can find out. It is about a couple of billion dollars. I do not know; it is probably more like \$3 billion. I will have to get the information on that.

**Senator SHERRY**—So the decline in consumption or the decline flowing from meat producers in the domestic market can be anywhere between \$20 million to \$30 million up to \$100 million, possibly higher.

**Dr McGovern**—I would say quite easily, yes.

**Senator SHERRY**—That is at a time when most beef producers, both for the domestic and export market, are not making any money at all, as I understand it.

**Dr McGovern**—Yes. What you are saying is consistent with the Centre for International Economics study that found that the way out for beef was to export more at a cheaper price.

**Senator SHERRY**—But you cannot do that at the moment effectively. You cannot export—

**Dr McGovern**—That was the model's answer.

**Senator SHERRY**—and get a better price. We have had some representations from some other agricultural groups—the Stone Fruit Association in Adelaide last week; we have got the banana growers this afternoon—in some respects expressing similar concerns. Senator Harradine in fact raised the issue I think last week in Adelaide—it might have been earlier—with the NFF. They were the first group that had ever come before him in his long political experience in the Senate that was advocating a tax on what they produce. There is an obvious impact, particularly if you are selling in the domestic market, through switching in consumption, and an associated decline in consumption of varying levels. What is your explanation of the NFF's position, given some of the concerns we have had, not just from you but from some other primary producers in this country?

**Mr Jeremy**—At the risk of being assassinated I have to say that the NFF is not in touch with producers these days. The NFF has been in Canberra for, I think, 21 years. None of the people there have to stand for election. It is a cosy existence and I would think that, if the NFF actually tripped over a few farmers one of these days, they would get a far different view to what they have. This is why we are seen as a small group in the scheme of things, because all our members have a belief that industry representatives should go through some sort of an electoral process so that you are sensitive to the needs of your members, and we are very sensitive. If I do not perform as a director I simply get shot out of business, the same as you senators yourselves will, whereas when you get to bureaucratic positions—I am

sure you fellows deal with these people every day of the week—where the cushions are very soft and the salaries are very high and you do not stand for election, the body runs its own agenda on policy, which has not necessarily got anything to do with farmers.

**Senator FERGUSON**—Can I just correct something, Senator Sherry. Are you suggesting that the President of the NFF is not elected?

**Mr Jeremy**—He is elected, yes.

**Senator FERGUSON**—And the branch president from South Australia is not elected, and the vice-president, and all the committeemen?

**Mr Jeremy**—No.

**Senator FERGUSON**—So when you are talking about ‘the NFF’ who are you referring to?

**Mr Jeremy**—I do not know how many people are in there, but they are fairly permanent appointments, aren’t they?

**Senator FERGUSON**—There are thousands of members. They are all part of the NFF too.

**Mr Jeremy**—The NFF’s view of farming and the farmers’ view of NFF are two different things, I can assure you.

**Senator FERGUSON**—Perhaps from your perspective.

**Senator SHERRY**—You believe that you are genuinely representing the range of people that you outlined earlier in your fears about a drop in consumption of beef as a result of a GST in this country?

**Mr Jeremy**—This is correct, and our predominant member is the cattle producer, but we have abattoir members. One of the major supermarket chains is a member and we are taking advice right through the beef industry without getting involved with the concerns of any other body.

**CHAIR**—Hansard has about one minute of tape left.

**Senator SHERRY**—I have two questions; hopefully you can answer them. Senator Ferguson referred earlier to the benefits of the cash flow that a GST gives you. Will you dash out onto the short-term money market and invest the odd few thousand in GST tax collections you have got for a couple of months and make a heap of money?

**Senator FERGUSON**—No, because most of them are paying interest.

**Mr Jeremy**—I cannot imagine that that will happen.

**Senator SHERRY**—Exactly.

**Senator FERGUSON**—It saves their interest bill.

**Senator SHERRY**—You do not see any benefit in that.

**Mr Jeremy**—No.

**Senator SHERRY**—Secondly, the administrative nightmare that you referred to, the increased administrative record keeping that you have to keep as a result of a GST: do you see that as being worse than the current paperwork you face with a wholesale sales tax?

**Mr Jeremy**—Yes, the wholesale sales tax regime is not really a worry to farmers. We have a number, and we quote our number to our supplier. Wholesale sales tax does not really worry the actual producer on the ground.

**CHAIR**—One more question.

**Dr McGovern**—Could I just state one quick point on the NFF. The NFF is systemically misinformed about the importance of exports to Australian agriculture and I can go into that further later on. They understand that 70 per cent goes offshore, but the actual figure is about 30 per cent. So their whole case rests upon misinformation.

**CHAIR**—Thank you very much for your assistance to our inquiry. You did indicate that you will be supplementing the submissions before us with some further notes. Is it your wish to have those additional notes incorporated in the record of this hearing?

**Mr Jeremy**—Yes, we could do that.

**CHAIR**—As part of the submission.

**Mr Jeremy**—Yes.

**CHAIR**—Is that agreed by the committee? Yes, it is agreed. That will be done.

**Senator FERGUSON**—And there was also an indication that you would supply us with the name of the accountancy firm that gave you the advice which we believe is not correct, so that we can contact them.

**Mr Jeremy**—Yes, I will do that.

**CHAIR**—Thank you very much once again. This part of the hearing is now completed.

**Proceedings suspended from 1.07 p.m. to 2.07 p.m.**

**MILGATE, Ms Margaret Ann, Market Development Officer, Queensland Fruit and Vegetable Growers**

**SIMPSON, Mr Christopher James, Executive Officer, Banana Sectional Group Committee, Queensland Fruit and Vegetable Growers**

**CHAIR**—I now resume the Senate hearing into a new tax system. The next witnesses are Mr Chris Simpson and Ms Margaret Milgate from the banana growers association. Welcome to you both. We will invite you to make a brief oral overview of your written submission and then be available to answer questions, if you would be kind enough to do so.

**Mr Simpson**—Thank you. To begin with, I would like to apologise for Len Collins, the Chairman of the Banana Sectional Group Committee, who is also Chairman of the Australian Banana Growers Council. We were only advised of the opportunity to appear before the Senate committee yesterday and Mr Collins, who is away from home base in Tully, was unable to get to Brisbane in time for this hearing.

**CHAIR**—We appreciate you making the effort to accommodate us.

**Mr Simpson**—With pleasure, Senator. The Banana Sectional Group Committee is the representative body of the banana industry in Queensland. The Queensland industry comprises about 800 banana producers. The industry is concentrated in the wet tropics region of Far North Queensland, basically between Townsville and Cairns and particularly the towns of Tully and Innisfail, and there are approximately 580 growers in that area. The Far North accounts for about 90 per cent of Queensland's banana production, which is about 75 per cent of Australia's total production. The remainder of the industry is in the south-east region, in the Caboolture district to the near north of Brisbane, the Sunshine Coast hinterland and there are some new developments in the Bundaberg district.

Queensland's total banana production in 1998 was 16.25 million cartons and they are 13-kilogram boxes, which represents 80 per cent of the Australian total. The gross value of production in 1998 was \$205 million, noting that prices were depressed last year, and in 1997 the GDP was \$236 million. In August 1998 the Banana Sectional Group Committee decided it wanted to assess the impact of the proposed GST on the banana industry. Accordingly the committee engaged agricultural economists, the Centre for Agricultural and Regional Economics, CARE, of Armidale in New South Wales, to model the likely impact of the new tax. CARE modelled the effects of the tax package on three banana businesses, which were a small banana farm which was in the southern region of Queensland—and 'small' is defined as less than five hectares; a medium producer from North Queensland—and a medium producer is in the range of 25 to 40 hectares; and a large banana enterprise, also in North Queensland, and that was defined as over 100 hectares.

The study modelled actual data supplied by these cooperating banana producing enterprises whose identities have been kept anonymous for commercial-in-confidence reasons. The model captured the total business level impact of the tax reform proposal and was not simply a partial model which focused on selected elements such as the GST. The model incorporated the following basic assumptions set out in the tax reform package

released by the Treasurer in 1998: a GST of 10 per cent across the board; the abolition of wholesale sales tax; the reduction of fuel excise and the inclusion of a GST, such that the pump price remains unchanged; diesel excise for off-road use remains fully rebated; an additional diesel rebate of 9.7c per litre for on-road diesel use for vehicles of GVM over 3.5 tonnes, leaving a road user charge of 18c per litre; changes to the social security system; changes to personal income tax rates in accordance with the proposed new scales; and changes in the tax treatment of trusts.

Overall, the impact of the tax reform package was positive for the banana growing enterprises examined in the study. Whilst elements of the package had a negative effect, such as the GST increases household costs, the net impact of the positive and negative effects when taken together is an improvement in financial performance. In more detail, the net disposable income of banana producers has increased, for small farmers 4.9 per cent, medium 9.4 per cent split between two partners and, for the large enterprise, 8.4 per cent. In terms of total taxes paid, the small producer's taxes fell by 4.6 per cent, the medium producer's rose by 9.9 per cent and the large producer rose by 3.2 per cent. The household expenditures rose by between 3.5 per cent and 3.6 per cent for all of the enterprises and the benefits accruing from reduced fuel excises were relatively small.

The benefits from reduced transport costs are a major contributor to improved financial performance for the medium and large enterprises. The extent to which the transport savings are passed on is, therefore, one of the most important factors for the northern banana industry and one of the issues we are highlighting in our submission. CARE also modelled the effects of retail pricing strategies in the implementation of the GST, which could lead to lower returns to producers. They found that a 10 per cent reduction in price received by growers would have a large negative impact on net disposable incomes as follows: for a small producer, his net disposable income could fall by 12.7 per cent; for a medium producer it is 55.7 per cent, which is a massive cut in income; and for a large producer, 32.1 per cent.

Given these findings, the BSGC submission to the Senate inquiry therefore focuses on the following two issues: the reliance on transport savings to be passed on for the tax package benefits to be delivered to the banana industry and retail pricing strategies which have the potential to leave the banana industry producers considerably worse off. I now turn to our written submission, Senator, and just highlight a few factors there focusing on those aspects.

**CHAIR**—Certainly.

**Mr Simpson**—Basically, we wish to emphasise in particular the potential for the intended benefits of the reform package to be undermined by the pricing strategies of the supermarkets. Our recommendation is that one of the administrative imperatives in the new tax package be—and we have quoted this in the introduction in section 1:

That full price transparency, that is actual plus full 10 percent GST costs, be displayed to consumers at the retail point of sale.

The reason for the need for this is outlined in the submission and its attachments.

Turning to section 2.1 on page 4, headed 'Importance for Savings in Other Sectors to be Passed On, it states:

Benefits from reduced transport costs were the major contributor to this improvement. However these benefits would be largely eroded if the savings were not passed on at the full 6.7 per cent rate forecast in the government's reform package papers.

For example, if the savings were not passed on, the GST benefits for a medium producer in North Queensland would be reduced from \$10,010 to virtually nothing—that is \$1,664—and for a large producer, also in North Queensland, from \$49,650 to \$14,154. For the smaller banana enterprise, which is in the near metropolitan area of Brisbane, the transport savings are not a significant issue.

The pricing effects: the banana industry is concerned that major supermarkets may attempt to maintain shelf prices at their current levels after the GST has been added on. The effect of this would be a reduction in the wholesale price paid to producers. The CARE report has analysed this possibility and, in summary, the small producer would experience a reduction in net disposable income of \$3,332, the medium producer would be hard hit with a 55.7 per cent drop in net disposable income or a \$59,394 cut in income, and the large producer would have his return slashed by 32.1 per cent or \$190,303.

Given the pricing effects findings of the CARE study as reported above, the BSGC is very concerned that the banana industry would be severely affected by the GST, as would be many other areas of primary production, particularly domestic market producers. Accordingly, the BSGC believes that pricing strategies of the supermarkets which they are likely to adopt post GST should be examined in some detail. As there is no wholesale sales tax on fruit to be removed, the full 10 per cent GST will have to be passed on to consumers by being added to the retail price of bananas, this being essential to the concept of any consumption tax.

The problem is that banana producers are not price setters but are price takers, and prevailing market prices are largely determined by the enormous duopolistic buying power of the supermarket chains. Producers have little ability to set the whole price, let alone add the GST, as they should in theory, and similarly no ability to ensure that the supermarkets pass the tax on to consumers.

In practice, the following scenario should be considered: using a hypothetical base retail price of \$1.99 per kilo, bananas priced at \$1.99 pre GST should be ticketed at \$2.19 post GST, namely \$1.99 plus 10 per cent GST. However, because of their pricing strategies—and we have demonstrated with some attachments of newspaper cuttings which I have brought along here which show how supermarkets like to have a 99c on the price of everything—the supermarkets will often want to round prices down to maintain the appealing price point. In other words, they might want to keep that at \$1.99 irrespective of the GST.

Such a pricing strategy would effectively reduce the base price, not to \$1.99, but back to \$1.79, and thus force a 10 per cent price cut back through the marketing chain to producers. In effect, producers would be picking up the GST rather than it being passed on to consumers. To highlight this point, on the ABC's *AM* radio program on 22 January there

was a report on new powers being given to the Australian Taxation Office to crack down on the avoidance of the GST. In response to a question about businesses paying their fair share of tax under the GST, Mr Michael Evans, tax partner at Arthur Andersen, stated, 'That's exactly the point, because business doesn't pay GST. A GST is a tax that's intended to be paid by consumers.'

In saying this, Mr Evans makes an important point that is not always well understood. The GST is intended to be a tax on consumers and consumers will receive an offsetting reduction in personal income tax to compensate. It is therefore essential that the extra tax revenue be generated from the consumer at the retail point of sale; otherwise the tax reform package will simply not work as intended. To overcome the potential adverse pricing effects for producers, the BSGC believes that the GST should be introduced with safeguards built in to protect banana growers and other commodity producers against the possible scenario outlined. The safeguard needed is for the GST to be implemented in a transparent manner as an add-on tax to the retail price of goods such as state sales taxes in the USA, rather than as an inbuilt, invisible component of the retail price as proposed. The BSGC is advised that the GST in New Zealand was introduced with an arrangement like this in place for the first 12 months.

To conclude, the BSGC is very concerned that the possible pricing effects of the GST could undermine the intended benefits of the tax reform package and, in fact, could leave the banana industry significantly worse off. The BSGC therefore believes that the package should be finetuned with the goods and services tax implemented as an add-on tax to the price of goods at the retail point of sale. If this approach is not taken, the BSGC is concerned that the tax reform Australia gets will not be the reform promised by government and, in the case of the banana industry, intended benefits will not be delivered. Thank you.

**CHAIR**—Thank you, Mr Simpson. Is it your intention to have Ms Milgate supplement your remarks, or is that it for the time being?

**Mr Simpson**—If she wishes to make further points—

**CHAIR**—I am not touting for it; I am just asking.

**Mr Simpson**—We had nothing further planned, but we are available to take questions and if Margie wants to make additional points—

**Ms Milgate**—I would just like to make the additional point, Senator, that we represent the Queensland Fruit and Vegetable Growers and, even though the study has been done on behalf of the banana industry, it is a concern that we are encountering across all of our industries. We are not just talking about bananas; we are talking about all the major fruit and vegetable growers in this state.

**CHAIR**—What is the value of your industry? Can you put a figure on it?

**Ms Milgate**—A billion dollars per annum. We supply most of the winter product into Sydney and Melbourne markets. We also supply year round most of the tropical fruits that are eaten by consumers, in southern markets in particular.

**Mr Simpson**—Mr Chairman, that figure is for fruit and vegetables. For bananas, as I said in the submission or my introductory remarks, the figure is \$205 million in 1998.

**Senator GIBSON**—That is retail price?

**Mr Simpson**—No, that is wholesale price, gross value of production.

**Senator GIBSON**—For the total banana industry?

**Mr Simpson**—Yes.

**CHAIR**—You have said in your submission to us that you effectively support the proposal that the government has put, but that you want safeguards built into that proposal—safeguards of transparency and a greater certainty that cost reductions that occur will be passed on to you promptly. That is essentially as I heard your submission.

**Mr Simpson**—Exactly. We want safeguards. I am not sure that promptness is a necessary aspect of it, though. As we have said, the tax is to be paid by consumers, so if the price is \$1.99, or \$2.99 at the moment, that price is established in the market by the supply and demand forces, but with a GST added it should be an extra 10 per cent to the consumer. As I said, to maintain the \$1.99 or \$2.99 price point there would be a lot of pressure on supermarkets to stick to that price level, which in effect would force that 10 per cent cut in price back through the marketing chain to the producer.

**CHAIR**—My question is this: the government has said it will not change its package. In the event that it does not in fact change its package, should the Senate, in your view, adopt the package without the changes that you are proposing should be made, or should it not? Should it reject it?

**Mr Simpson**—We are not opposing the GST; we are just asking for safeguards to be implemented, so I do not see that as a fundamental change to the package.

**CHAIR**—Can I just press you a little further on this. I understand that you are supporting the package and you would like these safeguards in. If the government declines to include them, do you still support the package?

**Mr Simpson**—Based on the CARE modelling, banana businesses are better off under the new tax proposal, so the banana industry would accept them.

**CHAIR**—Is that true of the fruit and vegetable industry?

**Ms Milgate**—They would be still very concerned about the reduction in income that could come from not having some more transparency in the system. The other major thing that was highlighted earlier by the banana report was the great savings in transport, and if these are also passed back on, there is a twofold reduction in income. So the industry would be greatly concerned if the package went through without those changes.

**CHAIR**—If I may, could I just press you a little further, because we have to actually vote on this and it would help us to know, when you come to a fork in the road, what the decision should be, in your view. I appreciate you are saying ‘greatly concerned’, but does that mean your support for the package is removed if your changes are not included?

**Mr Simpson**—Mr Chairman, I guess the pricing effects are a little bit outside the tax itself but, assuming implementation, they do show that the medium producers’ net disposable income would be reduced by 55.7 per cent, if that scenario became a reality, and for a large producer by 32.1 per cent. So we could not support that sort of scenario. But we are basing our support on the fact that what the government has promised in the tax reform paper is actually delivered in terms of the financial outcomes. I see the method by which it is delivered, and other taxes and add-ons to the retail point of sale, as not affecting the financial outcomes; it is just guaranteeing that that will happen.

**CHAIR**—Ms Milgate, on behalf of the fruit and vegetable people?

**Ms Milgate**—I think the whole tax package is still being considered by the industry, so I would not like to give you a definitive yea or nay at the moment to this, but I am just sort of saying that is one of the major concerns we have at this stage.

**CHAIR**—And is it your wish that these views be reflected in our report—that you would like these changes made?

**Ms Milgate**—Most definitely.

**Mr Simpson**—Very much so.

**CHAIR**—Okay. Senator Ferguson.

**Senator FERGUSON**—I just have a couple of questions before I pass to Senator O’Chee. You expressed some concerns about transport costs in your industry. What sets the cost of transport currently in your industry? How is the price determined of the costs of transport? What keeps it at the level it is?

**Mr Simpson**—I am not sure just how far I can go into the economics of the transport industry but from a banana point of view our industry is in Far North Queensland. It is nearly 2,000 kilometres from Brisbane and 80 per cent of our production is in that area. We supply to markets in Brisbane, Sydney, Melbourne, Adelaide, Perth and Tasmania, and transport costs are a huge component.

**Senator FERGUSON**—What determines that cost?

**Mr Simpson**—I guess the transport companies set their freight rates based on their capital cost plus the operating costs of their fleet. I guess it is the price that they are able to set.

**Senator FERGUSON**—Is there any competition in that industry?

**Mr Simpson**—Yes, there is, certainly. The transport companies are made up of lots of small and medium businesses just like the banana industry.

**Senator FERGUSON**—Do you think competition has any effect on the price that you eventually pay?

**Mr Simpson**—Hopefully it will.

**Senator FERGUSON**—I mean currently, today.

**Mr Simpson**—Yes, it does, and the transport companies are always saying that their margins are fairly tight. The package predicts that transport costs will be reduced by 6.7 per cent and we are depending on that 6.7 per cent to be passed on to the user. If it is not then I guess there is a temptation that it will not because the transport companies say, ‘We can’t afford to pass it along, we weren’t making money before.’

**Senator FERGUSON**—Why don’t they put their prices up today if they are not making money?

**Mr Simpson**—I did not say they were not making money.

**Senator FERGUSON**—If they are not making much, if the margin is tight, why do they not just increase their prices?

**Mr Simpson**—I think you would have to ask the transport industry that. I cannot really say.

**Senator FERGUSON**—Do you think competition might have something to do with it?

**Mr Simpson**—Yes.

**Senator FERGUSON**—The point I am trying to make is that if competition is setting the price today and they need a reasonable margin to survive, exactly the same process will determine what the costs will be after the introduction of a GST and so it is likely that it will be exactly the same margin because competition will force them to stay at that margin.

**Mr Simpson**—That is true to some extent, but I remember when I studied economics—which was a long time ago—micro-economic theory was that if you take a tax cut, the benefits will be shared between both sectors and it does not all go to the one place.

**Senator FERGUSON**—It seems like everybody has been to economics courses.

**Mr Simpson**—Unfortunately for you, Senator!

**Senator FERGUSON**—Not unfortunately at all, but the whole point I am trying to make is that if the market rate set today is determined by either one of two things—either the profit margin the transport company is prepared to accept, or the competition that forces

them to accept a certain level—after the introduction of the GST exactly the same forces will apply.

**Mr Simpson**—Probably not, really, because it is much easier to not pass on the reduction than it is to implement an increase.

**Senator FERGUSON**—So competition will not be there any more?

**Mr Simpson**—No. The competition will still be there, but before anyone jacks up their rates they would look long and hard at what the competition is doing. But a cut in prices, I guess, could be seen as a bit of a bonus to the customer of the transport companies, so the extent to which they feel obliged to deliver that bonus—

**Senator O'CHEE**—The problem for Mr Blennerhassett, of course, is that vehicles coming back from Cairns empty will take a back load in undercutting. That is why, when you talk about the North Queensland banana industry, you actually enjoy pretty good freight rates.

**Mr Simpson**—Yes. I am getting a little bit deep here, but one of the benefits the industry is always advocating—of the industry in the north—is that by supplying product to move down south, they can have backloading of other products to the north, which helps the economy in those areas overall.

**Senator O'CHEE**—In fact, the rate Cairns-Brisbane per kilometre is one of the most competitive in the country, is it not?

**Mr Simpson**—I would have to take your word for that. I am really not across the detailed economics of the transport industry.

**Senator O'CHEE**—The cost per tonne Brisbane to Cairns is \$100 a tonne. The cost Cairns-Brisbane is in fact a little bit less. These assumptions in the CARE model assumed a 6.7 per cent reduction in transport costs, but the Road Transport Forum on long-distance routes estimates savings of 15 per cent to 19 per cent. If you factored savings of that magnitude or even half of that magnitude into the CARE model, it would significantly alter the bottom line for producers, wouldn't it?

**Mr Simpson**—The CARE model really took the figures that were provided by the Treasurer's paper and modelled those in.

**Senator O'CHEE**—Sure.

**Mr Simpson**—I really cannot say anything other than that.

**Senator O'CHEE**—I do not want to get into why those figures are different, but we had evidence to say that for heavy road transport over long distances the savings are different because the PRISMOD analysis of transport includes taxis, you see. So the Road Transport Forum say their savings will be 15 per cent to 19 per cent over long-haul freight. I am just saying to you, if you accept that—because you have said that there are all sorts of different

possible outcomes—as a possible outcome then obviously it will have a substantial positive effect on producers, won't it?

**Mr Simpson**—If that is the case. As I said, we are not rewriting the government's assumptions or redoing the model, we are just taking the model with the figures given to us by the government. But if the savings are as you say and greater than the 6.7 per cent quoted, obviously our industry would be better off.

**Senator O'CHEE**—When my wife tells me to go and buy bananas I just go and buy bananas because the danger of not obeying her is too frightening, but what is the retail price of bananas in the store in, say, Brisbane or Sydney?

**Mr Simpson**—It has been around about \$1.69, \$1.79 or something recently, but with the cyclone in North Queensland we have just had a 70 per cent crop loss in the Innisfail district and a 50 per cent crop loss at Tully and bananas are going to be in extremely short supply through until about November. That will be impacted in the prices that are going to be seen in the shops through the rest of the winter as well.

**Senator O'CHEE**—What do you estimate they will be in the shops?

**Mr Simpson**—\$3.99, in a month's time.

**Senator O'CHEE**—But that indicates the price can be wholly variable, doesn't it?

**Mr Simpson**—Supply and demand. There will be very light supplies.

**Senator O'CHEE**—But the price at the moment has been \$1.69, you say, or \$1.79?

**Mr Simpson**—Yes, it has been quite low.

**Senator O'CHEE**—The supermarkets did not feel like they had to make it \$1.99, did they? They knew they could not get it.

**Mr Simpson**—Not at the moment, but \$1.99 is not an uncommon type of price. It depends on the supply and demand and, as I said, supply has been fairly heavy until the cyclone and prices have been quite depressed.

**Senator O'CHEE**—What I am getting at, of course, is the fact that supermarkets are not always going to make every price \$1.99, or \$2.99, or \$3.99. What really sets the price, as you say, Mr Simpson, is supply and demand, is it not?

**Mr Simpson**—That is right, but even if the price is \$1.69, we need to know that they will add 10 per cent.

**Senator O'CHEE**—It is just that when you look at the attachment you have given us, some items are 99c or \$1.99, but some are \$2.69 and some are \$3.69, one is \$1.39, apples are \$1.59.

**Senator FERGUSON**—Less than half are 99 cents.

**Mr Simpson**—Yes, but a 99-cent figure is still the majority of any of those other options.

**Ms Milgate**—Consumer research shows that most consumers just have a point they will not go above and a 99-cent figure gives them a bit more comfort. You do not want a \$2 level, or be under a \$2 level or a \$3 level, et cetera. When the prices start getting up towards a certain level they will stop, or drop off. They will perhaps still buy a product but maybe less of it, so you have problems in that sense. There is variation but there is also a level where consumers just know that they are not going to pay any more.

**Senator O'CHEE**—You also get seasonal variations, too, do you not?

**Ms Milgate**—Yes, definitely.

**Senator FERGUSON**—But \$3.99 surely—where is the ceiling for your price? Surely the availability of the product is really what is determining the price, is it not?

**Mr Simpson**—Yes, and I have never seen it higher than that previously, but if you had the GST it should be \$3.99 plus 10 per cent.

**Senator FERGUSON**—Not necessarily, because you do not know what savings you are going to have in the \$3.99. The base price might be less.

**Senator O'CHEE**—In fact, that is what the CARE document is saying to you. It is not necessarily going to rise by 10 per cent. That is what the document says.

**Mr Simpson**—Yes, but when prices are not going up by 10 per cent it is because there is a wholesale sales tax being taken off as well.

**Senator O'CHEE**—Or a transport component.

**Senator FERGUSON**—Transport component, all sorts of things.

**Senator O'CHEE**—And that is what the CARE document was really saying. They are saying, 'Look, there are a lot of inputs to the cost, transport being one of them, and by reducing the transport cost you reduce the in-store price of the goods and that changes the demand, and then that impacts on the net disposable income of the producer at the end of the day.'

**Mr Simpson**—Yes, but whatever the supply and demand determines, taking into account any other savings that are brought through the system, you still need to add the 10 per cent GST.

**Senator O'CHEE**—Yes, sure.

**Mr Simpson**—Because the 10 per cent GST would be added to manufactured goods, and it needs to be added to fruit as well.

**Senator O'CHEE**—Yes, sure, but what I am saying to you is that, say, it is \$1.79 now. It does not necessarily mean you are going to add 18c to the retail price. I think that is what we are discussing.

**Mr Simpson**—Well, whatever the price level, it would be determined under the normal laws of supply and demand. The 10 per cent should be added to that.

**Senator O'CHEE**—But what we are saying is that to work out the proper price you have got to look at the cost now, less the savings, and then add a GST. You accept that?

**Mr Simpson**—Yes.

**Senator O'CHEE**—Yes. One final question to you: the government has announced that the ACCC will be empowered to look at the pricing of goods in stores and concentrate particularly on supermarkets, with fairly substantial penalties of up to \$10 million for profiteering. Do you feel that those penalties need to be increased, or do you think the penalty level is sufficient?

**Mr Simpson**—I am not sure what the penalties are, but I really do not see that relating to the scenario we have presented here, because we are not talking about a profiteering scenario; we are talking about the opposite, which is the potential for the tax not to be passed on to the consumer. Also, you can only measure whether the 10 per cent has been added on, or another figure, if you know what your real base price was, and under the new situation it is going to be hard to determine what the real underlying price was.

**Senator O'CHEE**—It is just that all the welfare groups are saying that all the prices are going to be jacked up and the price savings will not be passed on, and you are here saying, 'No, they're not going to be passed on, but in fact there are going to be savings.' I just have a difficulty reconciling your view of the world with the view that my Labor colleagues have here that all the prices are going to go up. Why should we say that your view is better than, say, ACOSS?

**Mr Simpson**—We know that when buying bananas and many other products the supermarkets are pretty hard nosed, and it is very hard to get a better price out of them when they do not want to pay it.

**Senator O'CHEE**—ACOSS will be pleased.

**Mr Simpson**—I would just like to add one further point there. Going back to what I said before, the banana industry are price takers, not price setters, and a lot of manufactured goods are price setters, and that is the big difference.

**Senator FERGUSON**—Can I just go back to your submission, because I think there are a couple of things we really need to clarify. You talk about CARE doing the consultancy

work for you. In fact their study found that the tax reform package was ‘positive for banana growing enterprises’.

**Mr Simpson**—Yes.

**Senator FERGUSON**—Whilst elements of the package had a negative effect the net impact would still be an improved financial performance.

You still stand by that?

**Mr Simpson**—Yes.

**Ms Milgate**—Yes.

**Senator FERGUSON**—The other thing is, in talking about transport savings, if the full transport savings are passed on—and in fact, as I was trying to say, because of the competition factor, it is possible they will be, and some people will disagree, but it is possible—it means that a medium producer has a financial benefit of some \$10,000 per annum, a large producer up to \$50,000 per annum, and so in fact there is a considerable advantage to banana growers out of this total tax reform package, isn’t there?

**Mr Simpson**—If those are passed on, yes.

**Senator FERGUSON**—Even if nothing was passed on, there is still an advantage according to these figures: \$14,000 for large producers and \$1,600 for smaller producers. So there is a net benefit regardless of what happens.

**Mr Simpson**—Yes, but in percentage terms—

**Senator FERGUSON**—Well, this is what your submission says. It says that if nothing was passed on, which is an unrealistic scenario, it would be reduced from \$10,000 to \$1,664. For a large producer, if nothing was passed on—which is an unrealistic scenario—you are talking about it reducing from \$49,650 for a large producer to \$14,000. So there is a net benefit, regardless of what happens.

**Mr Simpson**—Yes, but we are talking about businesses worth millions and millions of dollars—

**Senator FERGUSON**—I understand that, but we are talking about a net—

**Mr Simpson**—so \$14,000 in percentage terms is really not a huge difference.

**Senator FERGUSON**—I understand that, but there is not a negative.

**Mr Simpson**—No.

**Senator FERGUSON**—There is a net benefit.

**Mr Simpson**—And we acknowledge that.

**Senator BARTLETT**—Do you have any idea, just sticking with bananas, what the elasticity is? If the price goes up 10 per cent, does that drop consumption by a certain amount?

**Mr Simpson**—It is a highly elastic commodity. In fact, when you do study economics they always use fruit and vegetables as the example of perfect competition—supply and demand and movement of prices with supply. We normally have not got the effects like the cyclone at the moment. It is not unusual for banana prices to range from less than \$10 a carton to up to \$30 a carton, based on fluctuations in supply as the year goes on. They are a highly elastic product. I just heard reports this morning that prices are moving above \$2 a kilo in Melbourne and there is a bit of buyer resistance creeping in there.

**Senator BARTLETT**—Right. As I understand from your submission and what you have said today, one of your big concerns is supermarkets not passing on the cost increase, and basically extracting it back out from the producer instead of the consumer, and you are suggesting that having the GST up front on the price tag would address that concern?

**Mr Simpson**—Yes, the base price would be for everyone to see.

**Senator BARTLETT**—You mentioned a number of times about being price takers and market prices being determined, particularly with supermarkets, by the market power they have got. Why would the fact that they have got \$1.99 plus 20c tax as opposed to \$2.19 or whatever openly seen on a price tag change the market power they have got to be able to screw the producer to as low a price as they like?

**Mr Simpson**—Can you just clarify that?

**Senator BARTLETT**—What I am getting at is that I would have thought the reason why they can screw the extra money out of the producer rather than the consumer is because of their huge market power, which is a widely acknowledged problem in the supermarket industry. It seems to me a bit strange that just forcing them to put the price tag split with the 10 per cent specifically displayed—particularly as, broadly speaking, most people would be aware that there is a GST there, assuming we tax food—would make such a difference to that pricing behaviour.

**Mr Simpson**—The way we see it is, if the ticket was the price plus the tax, if you go to the base price, that is the figure that will determine the wholesale price back through the chain to the producer, and if it is was \$1.99 before the GST and it was \$1.99 after the GST, you could see where the relativities are and what you get.

**Senator BARTLETT**—You would obviously be aware there has been a fair bit of debate about the issue of whether or not food should be included in the GST net. Do you have a view as an industry body about that?

**Mr Simpson**—Basically we are not asking for the GST to be removed from food. We have not modelled that so we do not have a firm view on it. But we take the position that if

it was not on food it would be a higher rate on everything else and, notwithstanding the fact that there are offsets and whatever, the producers would then be paying a higher rate on their cartons and fertilisers and all their other input costs. So, as I said, we have got a report that shows us that the across-the-board GST leaves the banana industry in a better financial position, so we are prepared to stick with that.

**Senator BARTLETT**—If the alterations to the package were not increasing the rate but modifying the compensation amounts so that you still would have the same costs and benefits as you do under the current package with the existing 10 per cent rate, would that affect your view on that at all?

**Mr Simpson**—I think we would have to get it modelled again to see what the outcome would be.

**Senator SHERRY**—If you look at the ANTS document, the cost effect by industry on fruit and vegetable products, \$21.03, is minus four per cent. Why have you used just the transport component of minus 6.7 per cent in your modelling?

**Mr Simpson**—I am not familiar with the document you are referring to.

**CHAIR**—It is the government's taxation document.

**Mr Simpson**—Right.

**Senator SHERRY**—It analyses the cost effect and then the price effect once the GST is added on, industry sector by industry sector.

**Mr Simpson**—Yes.

**Senator SHERRY**—Now, I would have thought it would be more logical for you to use the cost impact—pluses and minuses and indirect tax reform—as contained in this document, rather than just the transport component, because transport is not the only cost impact on your industry.

**Mr Simpson**—That is true. I should say that the figures used in the model were selected by the consultants, so they determined that 6.7 per cent was the figure to use and we were happy to accept their expert advice on that.

**Senator SHERRY**—The figure of 6.7 per cent is in this document as the cost effect for transport as an average. What I am just drawing to your attention is, I think you should have at least modelled or included the overall cost effect on your industry, which is obviously fruit and vegetable products.

**Mr Simpson**—The study was not on the industry. The study was on—

**Senator SHERRY**—On bananas.

**Mr Simpson**—three individual farms and these were the real costs that the three farms would have faced.

**Senator SHERRY**—You may care to consider this: I put to you that a valid figure to use would be the four per cent figure, just as much as the 6.7 per cent. But you might care to do some remodelling based on that figure. Just moving from cost to the final price, if we look at the effect on price of fruit and vegetable products, which is \$21.03—and this is assuming best case scenario; all cost reductions flow through and the big supermarkets do not put the squeeze on the producers—prices go up by 5.7 per cent in fruit and vegetables. That is again in this document. I do not necessarily accept the validity of those two premises but that is the likely smallest price on average across fruit and vegetables.

**Mr Simpson**—That would sound to be logical, based on the points that Senator O’Chee was making, in that the 5.7 per cent would be the increase that consumers would pay and then the 4.3 per cent below the line would be the savings that would occur on the production end.

**Senator SHERRY**—Yes. Now, you have raised, I think, two concerns or fears or risks. One is that, at least by the fact that you are here, you appear not to believe that all the transport costs, for example, or all the cost reductions are going to be passed on. Why do you believe that—that they are not going to be passed on in part or full?

**Mr Simpson**—I do not think it is the case that we do not believe it. We are just saying that the savings are highly sensitive and the extent to which they are not passed on would reduce the benefits of the package to the industry.

**Senator SHERRY**—But the government says they will be passed on; perfect competition out there in the market—‘She’ll rip along. They’ll all reduce their prices tomorrow, 1 July, 2000. The magic rule is here! Full competition!’ This is the government’s argument. It is not mine.

**Senator FERGUSON**—We have converted Senator Sherry.

**Senator SHERRY**—Don’t you have total faith in the government’s position: full competition tomorrow, all these price reductions right through your inputs? Why not?

**Mr Simpson**—I am too cynical to be an economic rationalist, I think.

**Senator SHERRY**—I put it to you that you have had some experience of the real world.

**Mr Simpson**—I guess so, yes.

**Senator SHERRY**—And real world, I would suggest to you, is that the price reductions, if they occur, are going to occur over time and at different levels and different circumstances.

**Mr Simpson**—Yes.

**Senator SHERRY**—Is that what you believe?

**Mr Simpson**—I guess that is a scenario that makes sense.

**Senator SHERRY**—Yes. Your other concern is the major retailers. Do you have any experience of the retailers pressuring banana growers on price?

**Mr Simpson**—I have not had any personal experience. I am not a banana trader.

**Senator SHERRY**—No, obviously, but you are representing the organisation.

**Mr Simpson**—But the pressure on price happens every day. There is the wholesaler in the middle and the wholesaler is the person who negotiates with the supermarkets and the grower really has no involvement in that negotiation process. As I said, the grower is the price taker, not the price setter.

**Senator SHERRY**—So if you had a combination of a failure to pass on full cost reductions and a combination of the large supermarkets—I do not know about this state; I assume it is an oligopoly, two majors with some localised competition—you have a risky scenario based on those two factors.

**Mr Simpson**—I believe we do. Supermarket concentration is probably more so in Queensland than in the other states, but that is the whole point of this submission. We do believe there is a risky scenario. We are not opposing the GST, but we are asking for safeguards.

**Senator SHERRY**—We have talked a bit about bananas. The fruit and vegetable industry and the issue of costs, cost reduction: presumably costs are different across the state because obviously some producers would be further from urban areas than others. Is it also the view of fruit and vegetable growers in general that there may not be a full pass-on of cost reductions?

**Ms Milgate**—Since the banana study was done that has been discussed by other committees of the organisation, and the board has taken a position that they have these major concerns as well, yes.

**Senator SHERRY**—So you believe the example in the study of banana growers is relevant to fruit and vegetables in general?

**Ms Milgate**—Yes.

**Senator SHERRY**—What about the issue of supermarkets putting the squeeze on prices?

**Ms Milgate**—There would be the same activities as there are for bananas, as there are for other fruits and vegetable products, yes. There is the risk there that to keep the prices competitive at their level, with the GST added on, that they will not take that risk themselves and pass it back to us. That is what the concern is of the industry.

**Senator SHERRY**—I know this answer for bananas, but you might care to give us the answer for the record, but with other fruit and vegetables, what proportion is exported from Queensland across the industry?

**Ms Milgate**—Sixteen per cent. That is out of Queensland directly. If you actually take out what is taken out of the floor in Sydney and Melbourne markets, I would say it would be much higher and I use the round figure of a billion dollar industry. Probably about \$100 million is actually exported products—is found elsewhere—so that is higher than the \$16 million. It is about \$100 million, I think.

**Senator SHERRY**—And bananas?

**Mr Simpson**—You said you know the situation. The banana industry seems to be a domestic focused industry. The world banana trade is dominated by companies like Naboa from Ecuador.

**Senator SHERRY**—Chiquita.

**Mr Simpson**—Chiquita, Dole—these companies—and most of the production comes out of places like South America, the Caribbean, the Philippines and the like and we cannot compete with \$4 for an 18-kilo carton of first-class bananas on a world market.

**Senator SHERRY**—You are fortunate you have got those quarantine protections.

**Mr Simpson**—There are some nasty diseases around the world.

**Senator SHERRY**—Is there still black sigatoka roaming around out there somewhere?

**Mr Simpson**—We have a spot outbreak every year, Senator. We had one farm totally eradicated last year.

**Senator SHERRY**—You say in your submission the GST is intended to be a tax on consumers.

**Mr Simpson**—It is a consumption tax.

**Senator SHERRY**—Yes. Do you believe that the 10 per cent GST in the case of your industry will be solely borne by consumers?

**Mr Simpson**—No, the producers will pay their share of the tax through buying their fertilisers, their cartons, their chemicals and their transport and all their other services.

**Senator SHERRY**—But they get a rebate.

**Mr Simpson**—Yes, they do get them rebated but at the end of the day there is still an amount of tax that they will pay too.

**Senator SHERRY**—But on this issue of micro- and macro-economics, we had a previous submission from the Australian Beef Association. They argued that the cost is shared between producers and consumers in terms of the cost to industry.

**Mr Simpson**—The study showed that the total taxes paid by the medium banana producer, if you recall, increases by—I think it was 9.9 per cent. I will just confirm that.

**Senator SHERRY**—But it is closely related to large supermarkets effectively forcing banana growers to accept a lower price.

**Ms Milgate**—The basis of our submission from the banana industry is that concern, that risk there. So we will not enjoy the full benefits of the package into the banana businesses.

**Mr Simpson**—Yes, the total taxes paid, if I can go back to that: for the medium producer it rises by 9.9 per cent, a large producer by 3.2 per cent, and for a small producer his tax rates fall by 4.6 per cent. So the producers will be paying more tax notwithstanding the rebates that will apply.

**Senator SHERRY**—Just going back to those figures you gave earlier of a small producer facing a potential net disposable income reduction of 12.7 per cent; medium sized 55 per cent reduction, that is \$59,000; and a large producer a net disposable income reduction of 32.1 per cent or \$190,000: it is a big risk, isn't it, if it does not go as it is assured by the government?

**Mr Simpson**—Yes, exactly, and that is the key point as to why we are here.

**Senator SHERRY**—Just finally, Senator Bartlett asked you about full price transparency. You say in your submission:

That full price transparency, that is actual plus full 10 per cent GST costs, be displayed to consumers at the retail point of sale.

There may have been other submissions that have made this point; we might have one to date I think that has suggested this. Are you sure that this is going to adequately address the concerns that you have outlined?

**Mr Simpson**—I think it is the safeguard that we need. Another way of doing it is for all products to be sold without the tax shown at the supermarket and then the tax to be added on at the checkout. The computerised checkouts can easily do that, just 10 per cent on the total bill, something like that. But basically we think the price plus tax is the best way to do it.

**Senator FERGUSON**—There was one answer that you gave to Senator Sherry. Senator Sherry asked you a question, I think, about the price sensitivity of your product and the fact that there was pressure from major wholesalers that affected the price of your product; in other words, there was a downward pressure. I think you said it is currently about \$1.69 in supermarkets. If that is the case, why is it going to rise to \$3.99 if they control the price?

**Mr Simpson**—As I said, we had a major cyclone which has caused probably the biggest damage in 20 years in the industry in North Queensland, with 70 per cent crop loss in Innisfail and 50 per cent in Tully. Bananas are going to be in extremely short supply. At the moment we are still clearing out a lot of the bananas that have been damaged by the cyclone but we are still there.

**Senator FERGUSON**—I think that clarifies the position. In fact, it is not the big supermarkets that are setting the price; it is the law of supply and demand, isn't it? When there is a shortage in supply, the growers actually have some pressure in forcing the prices up because of the lack of quantity that is available. So it is not really the large supermarkets. It is the supply and demand that actually determines at what level the price will be, isn't it?

**Mr Simpson**—Not entirely. I am not disputing that prices do not rise with supply and demand, because they do and they always have. But, once again, if you study economics there are different models.

**Senator FERGUSON**—I have no intention of studying economics.

**Mr Simpson**—There is the model of perfect competition, and then there is the monopoly model and there is an oligopoly model. There are different models. We are talking about the perfect competition model and applying it to duopolistic situation, and you just cannot do that.

**Senator FERGUSON**—I would suggest to you that bananas might be only \$2.99 if we are not in a world of perfect competition and supply and demand, instead of \$3.99. So don't frighten the market, will you?

**CHAIR**—Mr Simpson, you are a very courageous man, I have to say. You are here telling us that your product which is now untaxed should be taxed, and the reason why you are saying it should be taxed is that you believe the government when it says it will reduce other input costs to make it beneficial on your modelling and, on the assumptions your modelling is worked out on, to your producers. How confident are you really that all of those things will last forever?

**Mr Simpson**—If I can just go back to your first statement there, we are not saying our product should be taxed.

**CHAIR**—You are. They are not taxed already. Bananas are not taxed at the point of sale now, are they, Mr Simpson?

**Mr Simpson**—There is no wholesale sales tax.

**CHAIR**—No, and they are not taxed at the point of sale, but what you are saying is you agree to a proposition in which they will be taxed at the point of sale by 10 per cent. You support the package. You have said that yourself.

**Mr Simpson**—Yes. The government has said that it wishes to tax our product. We have had it modelled and it says, 'You'll be better off because of the totality of the package.'

**Senator SHERRY**—If all goes well.

**Mr Simpson**—So we are accepting that.

**CHAIR**—At the point of the introductory offer the government is saying, ‘Here’s the package.’ I think there are some substantial questions over whether your modelling is true or not, but only time will tell. People can model away to their heart’s content, but the real world takes over eventually, and you find out after the deal is done. But accepting all your modelling is true, how confident are you that all of those input costs on fuel and other things will remain down permanently? Governments do come and go, you know.

**Mr Simpson**—I am not sure it is a matter of whether I am confident or not. I think we have got a model that says, ‘This is the outcome that will happen,’ and Senator O’Chee has assured us that these things will come to fruition.

**CHAIR**—I will conclude my questions at that point. If it does not come good though, you will have to explain it to your producers, won’t you?

**Mr Simpson**—Yes.

**Senator HARRADINE**—A lot of the banana growers are family businesses, aren’t they?

**Mr Simpson**—Yes, very much so. We have got a number of very large producers in the Tully area, but in the Innisfail area we have got a very large number of small family businesses. In the South Queensland area the industry is on the decline in these urban fringe areas, but they are very small growers and they are family people.

**Senator HARRADINE**—Many of those would have family trusts, wouldn’t they?

**Mr Simpson**—I would imagine so.

**Senator HARRADINE**—Are you telling this committee that you are all foursquare on the government tax package which deals rather heavily with family trusts?

**Mr Simpson**—I really cannot comment on that. I have not studied the family trust scenarios.

**Ms Milgate**—Of the three businesses that were modelled, two of them were trusts. The medium and the larger sized businesses were trusts. The smaller, which is the majority, were not; there was a partnership.

**Senator HARRADINE**—So did you ask them the question as to how they felt about their entity being taxed as a company?

**Ms Milgate**—Senator, that was not the question that we gave to the growers. We modelled three different scenarios and their finances currently, now, and then all the assumptions were put into the model to see where they came out. We have not asked specific questions of the industry in the vein you were just referring to.

**CHAIR**—I think we are all done. Thank you very much for the assistance you have been able to provide to our inquiry.

**Mr Simpson**—Thank you, Mr Chairman. Thank you, Senators.

[3.07 p.m.]

**HALMARICK, Mr John Edward, Corporate Affairs Director, United Distillers and Vintners (Aust.) Pty Ltd**

**MULLER, Dr Robert Louis, General Manager, Bundaberg Distilling Co. Pty Ltd**

**PARLETT, Mr John James, Senior Manager, Tax and Industry Policy, Ernst and Young, on behalf of Bundaberg Distilling Co. Pty Ltd**

**CHAIR**—Welcome, gentlemen. Is it to you I should throw the call, Dr Muller?

**Dr Muller**—We will share the questions, but Mr Parlett will open.

**CHAIR**—I am sure you have been briefed, but the standard way of proceeding is for us to invite you to give us a brief synopsis of your written submission and then make yourself available, if you would be kind enough to do so, for questions from the committee.

**Mr Parlett**—Thank you, Mr Chairman, and thank you for the opportunity to appear before your committee today. We thought, Mr Chairman, if it is all right with the committee, we might share making our opening statements. Dr Muller will spend a few moments giving you a background to Bundaberg Distilling Co. and the market in which it operates. Mr Halmarick will spend some time talking about the broader level issues as regards alcohol taxation, and I will spend some time on the specific issue on which we appear before you today regarding the differential between the excise rate for Australian produced rum and brandy.

**Dr Muller**—Senators, as we have outlined in our submissions, Bundaberg Distilling Co. is one of the oldest companies in the alcohol business in Australia. It is over 110 years old, having been founded in 1888. It is a 50 per cent shareholding owned by Bundaberg Sugar and 50 per cent owned by United Distillers, of which Mr Halmarick is a representative here today. It is the largest producer of distilled spirits in Australia and, in fact, most of the rest of the distilled spirits industry is actually brandy production. There is another small producer of rum and virtually the rest of the distilled spirits industry in Australia is brandy production.

Rum is produced by the fermentation of molasses which is a by-product of raw sugar manufacture. It is very much analogous to brandy in that regard, in that it is an important ancillary operation of an important primary industry in Australia. That is the basis for our submission, really, in that we believe the preferential treatment that brandy has received over the years should equitably be shared for rum production in Australia. Bundaberg is not just a manufacturer of rum; it has made the city of Bundaberg synonymous with progress, really. As well as being the product, it has become the name of the city, or vice versa, so that if somebody asks you where you come from and you say Bundaberg, they know, wherever you are in the world, that that means rum.

**CHAIR**—It also means there are polar bears there, doesn't it?

**Dr Muller**—Polar bears are the secret weapon.

**Senator O'CHEE**—They know how to have a good time!

**Dr Muller**—That's right. It is an important part of the tourism industry in Bundaberg and in Queensland as a whole. Over 60,000 people a year come to visit the distillery, so it contributes in a significant way to the general economic progress of its local community and to the region. Bundaberg has been a progressive company. It has extended its product line significantly in recent years with products such as Rum and Cola, Dark and Stormy, Bundaberg Black, Bundaberg Royal Liqueur and Bundaberg Premium. It has a history of innovation and it is a company which is always ready to advance new technologies and new products.

One of the important things that should be noted in reading our submission is who our competitors are. We are quite emphatic that our competitors are not the brandy industry in Australia. We have spent a lot of money on market research and a lot of money in understanding who our consumers are. One of the specific things we find out about our consumers is what are the competitive products they consume. In the case of rum consumers, the competitive set is actually beer and other spirits, predominantly imported whiskies and predominantly American whiskey or bourbon.

Very few rum consumers are consumers of brandy and any change in the taxation position which is afforded to the rum industry would have a negligible flow-on effect to the brandy industry. That is a point we would like to make very clearly at the outset. I will pass over to my colleague, Mr Halmarick.

**Mr Halmarick**—I think it is probably obvious to most of us that spirits are heavily taxed compared to other forms of alcohol. In the government proposals it states that they recognise that spirits are highly taxed and they do not wish to see any higher taxes. However, there are issues in relation to the full tax on spirits, and there are a lot of them which need to be addressed and will be addressed tomorrow, I understand, by the Distilled Spirits Industry Council.

However, apart from that, we do applaud some of the government proposals, particularly in the area of the ready to drink beverage market, where the government proposes that alcoholic beverages at 10 per cent or less, other than pure wine or beer, are taxed at a beer rate which would have a significant benefit to Bundaberg itself, because they have a product called Bundaberg and Cola which is in that category. It would have some benefit. However, the other area the government continues to recommend to propose is that brandy has a preferential excise rate of reasonable proportions, and we cannot see the logic, if a government continues to wish to have a preferential rate for a spirit made from grapes, why they cannot recognise that a similar situation should exist for spirit made from Australian sugar, hence the reason we are here.

**Mr Parlett**—I guess in comparison to other issues your committee is dealing with and has taken evidence on, particularly in the first stage of your hearing process, the issue that we present before you on today could be considered to be relatively micro. Even so, the issue which our submission deals with—that of the taxation concession that exists only for

domestically produced brandy and no other spirit—is an integral part of the regulatory environment in which Bundaberg and other Australian producers operate. It is part of the industry's economic framework that influences and impinges upon business decisions and business outcomes. In this way Bundaberg considers the issue to be a relatively important macro one for it.

Tax policy is, to some extent, an instrument of the government to create the right environment for business entities to function, grow and add to the economy to generate positive economic outcomes. The point of Bundaberg's submission to the committee, and the reason for our appearance today, is to highlight what we believe is a tax policy anomaly that creates competitive disadvantages and distorts economic behaviours. The anomaly is implemented at the legislative level through the Excise Tariff Act for locally produced product, and through the Customs Tariff Act in respect of imported product.

At present those acts impose an excise duty of \$37.47 per litre of alcohol on most spirits including rum. In respect of brandy, however—locally produced or imported product including cognacs—the current duty rate is \$32 per litre of alcohol. There is thus a difference of \$5.47 per litre of alcohol or about a 15 per cent competitive advantage to brandy per litre of alcohol. As you know from our submission, Bundaberg's suggested solution to this excise anomaly is quite simple. The government has made it clear in its policy document that the concessional excise rate for brandy will remain below that applying to other spirits. In electing to continue the concession it is apparent that the government is recognising and endorsing policy drivers underlying the concessional brandy rate.

Bundaberg acknowledges and understands the policy driver and, furthermore, it supports the underlying policy principles that govern the brandy concession. It does so, because as Dr Muller has outlined, it understands the parallels that exist between the brandy production and rum production. Accordingly, it is our contention that the reduced excise rate proposed for brandy should also apply to Australian produced rum.

Mr Halmarick has already indicated that we are happy to see the removal of some other anomalies in the alcohol tax system, in particular in the ready to drink market where Bundaberg has a substantial number of products. Those anomalies were shown to distort investment and production behaviour and ultimately consumption behaviour. The anomaly in respect of the taxation of brandy manifests itself quite simply in that the excise duty payable on a 700 millilitre bottle of brandy is approximately \$8.29 while on a 700 millilitre bottle of Bundaberg rum it is approximately \$9.70—same alcohol content, same volume of liquid in the container. This discrepancy of course is compounded when it comes to adding the 37 per cent sales tax at the wholesale level when each product is sold.

The reason why we strongly recommend that the lower brandy rate be applied to rum is the underlying policy criteria that saw the introduction of the duty concession for the brandy industry, which we believe is equally applicable to the rum industry. Bundaberg sees the fundamental policy drivers for the brandy concession as being, firstly, there is a concession aimed at the production of high local content beverages produced from locally grown rural crops and, secondly, it supports an often volatile primary production sector.

The parallels with the rum industry to us are obvious. We have already heard from Dr Muller telling us that the production of rum involves a fermentation and then a distillation process, a process that is also followed in brandy production, only with grapes rather than molasses. The production of both beverages supports an important primary production sector of the Australian economy, providing a buffer market to what is often in each case a very volatile sector. Both industries are rurally based, providing significant employment opportunities in regional areas.

I think we have dealt with the taxation efficiency and equity arguments in our submission, and I do not believe we need to readdress them here. We would simply conclude by observing that brandy and rum are the only two major spirits produced in Australia today. When viewed at a broad level the production process for both beverages is very similar and provide an important stimulus to Australia's rural industries. The government has decided for policy reasons to maintain the brandy concession in the Excise Tariff Act and in the Customs Tariff Act after tax reform. With rum as the only other major spirit produced locally, this policy setting is to the rum industry's and Bundaberg Distilling Co.'s detriment. We recognise and support the policy drivers for maintaining the concessional excise duty rate for brandy and we simply ask, given the broad similarities between our sectors, that the same taxation setting be provided for the rum industry. We welcome your questions.

**CHAIR**—Thank you. In your submission dated 29 January you say there will be a more fulsome explanation later, and then you have another document dated 12 February, is that what you are referring to?

**Mr Parlett**—That's correct.

**CHAIR**—And both of them make almost a one-line recommendation for the excise duty rate for Australian produced rum to be set at the same concessional rate as Australian produced brandy. Is that all you are asking us to do?

**Mr Parlett**—Yes.

**CHAIR**—How much will it cost the government in revenue if it does that? Do you know?

**Mr Parlett**—We have done some rough estimates and we would be pleased to work with the Treasury people in some of the more sophisticated economics in terms of price and cost elasticities, but we believe it is in the order of about \$8 million.

**Senator FERGUSON**—It depends whether you increase the excise on brandy or decrease it on rum, doesn't it?

**Dr Muller**—There will actually be a net increase in excise collection across the spirits industry of over \$50 million. In fact, we have estimated approximately \$70 million, which will more than compensate for the small compensation.

**CHAIR**—Sorry, do I understand that if you reduce your excise down to that of brandy there is a net overall increase in revenue?

**Dr Muller**—No, there is a net overall increase in revenue because of the restructuring of the tax system. The spirits taxation level has been set to accord neutrality at the level of one product, namely Johnny Walker Red Label. Products that are currently sold at a price lower than that will in fact have an increase in price.

**CHAIR**—This is a \$30 billion tax package; \$8 million does not seem a large amount. What reason does the government give to you for not doing this?

**Dr Muller**—We would be interested to know.

**Mr Parlett**—None, really.

**CHAIR**—You have had discussions with them, though?

**Dr Muller**—We have advanced this proposal a number of times to various inquiries over the years.

**Mr Parlett**—Probably the most recent time that we have taken it forward was back in the beginning of 1997 when the Bundaberg Distilling Co. made a pre-budget submission at that time. I do not know whether you can recall—

**CHAIR**—So what did they say?

**Mr Halmarick**—The comments back from the government were that (a) they do not intend to take the preferential rate of brandy off, and (b) they do not intend to change the rate for rum, so it was status quo.

**CHAIR**—But they told you in reply to your entreaty that they are not going to change what they do, but they never provided any explanation to you as to why they are not going to change it? Is that right?

**Mr Halmarick**—That's correct.

**CHAIR**—It makes it a pretty difficult argument if you cannot get the reasons to grapple with. From what you are saying—and I must say when I read your submission it was new to me—we are providing an advantage to foreign competition over locally produced product here, given the nature of your market.

**Mr Halmarick**—Yes.

**CHAIR**—And at the very least it ought to be a level playing field and currently it is not.

**Mr Halmarick**—Yes, exactly.

**CHAIR**—There was a time when I would turn to the government and ask them to do something about it, but I am not in that happy position any longer, so I will turn to you, Senator Ferguson.

**Senator FERGUSON**—Perhaps I could preface my question by wondering why the previous government did not remove this disparity in the first place, then it would not be a problem for us. Perhaps, Senator Cook, you might be able to enlighten us as to why the previous government did not remove the disparity.

**CHAIR**—I do not know and, as I just said, that is the first time I have ever heard of this, I'm sorry to say.

**Senator FERGUSON**—I had better declare a conflict of interest as I come from a state which grows 50 per cent of Australia's grapes and so you can understand that I have some constituents that also make representations. Look, it is fair to say your position has been very consistent over a long period of time—I think along with the DSICA's quite frankly.

**Mr Halmarick**—Yes.

**Senator FERGUSON**—They have given evidence to lots of committees that I have been on. While the government is still retaining the disparity, it is a fact that they have actually increased in this tax package the excise on brandy, so in fact the disparity is lessening, isn't it?

**Mr Parlett**—I think the document says that the brandy rate will increase but it will remain below that for other spirits. I have not seen exact figures on that.

**Senator FERGUSON**—It does and I can actually quote the document to you because I just checked it with Senator Gibson then. The rate has increased. The current tax on a 700 millilitre bottle of brandy is \$12.82. It is going to increase to \$14.44, which is an increase of \$1.60 or something like that in tax per bottle. Whereas with whisky or rum or anything else it is going to increase by about 20c, the total tax take. So in fact there is a closing of the disparity, but certainly not to the extent that you would want it closed. I understand.

**Mr Halmarick**—Spirits are going to be going from \$37-odd to \$53.20 a Lal, and brandy from \$32 to \$47.97, so there is still between \$53.20 and \$47.90, there is still that gap.

**Senator FERGUSON**—Yes, I understand.

**Mr Halmarick**—Which equates to a couple of dollars a bottle at retail for the consumer, and this is one of the problems for rum vis-a-vis some of the lower priced bourbons and so on which are able to be sold at a lower price. There is another anomaly which is all to do with food standards and what is true bourbon but that is another question for another place.

**Senator FERGUSON**—This issue has been raised on a number of occasions with other committees that I have been on in relation to designer drinks and P6's and all—

**Senator CONROY**—P5's.

**Senator FERGUSON**—P5's and P6's, and in fact it is an issue that the government has been grappling with. If we are going to find out why in fact this disparity has not been

removed, we might have to go back and look at some of the reasons why the previous government failed to remove it, and then I might be able to give you an answer.

**Senator O'CHEE**—Can I ask, what is the volume of brandy sold in Australia in litres a year?

**Mr Parlett**—We have the figures in litres of alcohol. It is about 1.6 million litres of alcohol or about eight per cent of the total spirits market.

**Senator O'CHEE**—How much of that is Australian content brandy?

**Mr Parlett**—The figures as split between local and import is roughly 60 to 40, with 60 per cent in favour of locally produced.

**Dr Muller**—About \$A1 million.

**Senator O'CHEE**—How many litres of alcohol, of rum, is sold in Australia every year?

**Mr Parlett**—About 2½ million litres of alcohol or 12 per cent of the total spirits market.

**Senator O'CHEE**—How much of that is Australian content?

**Mr Parlett**—Seventy-nine per cent.

**Dr Muller**—So the Australian content is about twice that of the brandy industry.

**Senator O'CHEE**—There are really only two bulk uses you can put molasses to, aren't there?

**Dr Muller**—By and large, yes.

**Senator O'CHEE**—One is stockfeed supplements and the other one is rum, isn't it?

**Dr Muller**—Fermentation, yes.

**Senator O'CHEE**—Whereas with grapes you have got different uses for them. You can put it either to wine or to brandy, can't you?

**Dr Muller**—Yes. A lot of the brandy that is produced today also is produced as a by-product of wine production. It actually is made from grape marc, the seeds and skins left after fermentation. So to a lesser extent today, brandy is actually made from grapes. It is usually after the wine has been made that the brandy is produced. That is different from the way it was several years ago where grapes were grown deliberately for brandy production. That tends not to be the case so much today.

**Senator O'CHEE**—So in that sense the production of brandy today is even more analogous, I guess, to the production of rum.

**Dr Muller**—Yes. It is more like a by-product.

**Senator O'CHEE**—One of the concerns people might have, you see, is they might say, 'Well, look, there are really only two local producers of rum; there's Bundaberg and there's Beenleigh.' They might say, 'Well, look, this is really giving a lot of advantage to one big company, whereas if we keep the regime, then the advantage is spread amongst a lot of smaller producers.' How would you answer that one?

**Dr Muller**—Of brandy?

**Senator O'CHEE**—Of brandy.

**Dr Muller**—In fact there are not a lot of small producers of brandy.

**Senator O'CHEE**—Who are the local producers of brandy?

**Dr Muller**—There are just a number of relatively large—I think four or five would pull it up altogether. Tarac, I think, is the largest; Hardys, Seppelts, Tolleys.

**Senator O'CHEE**—If you separate brandy from other spirits, how many litres of alcohol of other spirits are sold in Australia, including rum?

**Dr Muller**—Brandy is about eight per cent of the total spirits sold in Australia. Do you want it in volume?

**Senator O'CHEE**—Yes, total volume.

**Dr Muller**—About 20 million litres.

**Mr Parlett**—Total about 25 million Lals, is it, John?

**Dr Muller**—About 20.

**Mr Halmarick**—I have not worked that out. I know there are about six million cases.

**Mr Parlett**—It is on page 4 of our submission—about 20.3 million Lals.

**Senator O'CHEE**—So brandy is a very separate market, you are saying then, from the other spirits? If I were to go into the Cattleman's Bar at the Exhibition and order a rum and Coke, nobody would think that would be terribly strange, but if I were to walk in and ask for a brandy in the Cattleman's Bar, people might think I was a bit peculiar, mightn't they?

**Mr Parlett**—They probably would at the Exhibition.

**Senator O'CHEE**—Thank you very much.

**Mr Parlett**—It is a niche of the market, yes.

**Senator BARTLETT**—With any tax system, obviously it is beneficial, particularly from this side of the table, to be able to explain to the public why it is the way it is and I think your lack of ability to get an answer on that one highlights a major concern. You would be aware of the DSICA submission as well. I notice your two companies are on the front page of that. I assume you are supportive of that as well. We will not go into that because that is for tomorrow. But there is one thing mentioned in there, which I have had pointed out to me before and which I found fairly astonishing, and that is this new loophole in relation to high alcohol products being sold as food essences.

**Mr Parlett**—Yes.

**Senator BARTLETT**—Does any of that substitution affect your market at all?

**Dr Muller**—Yes. There are products sold as rum essence which can be bought. They were not excisable up until recently. Certainly in a number of states they were purchasable in supermarkets. They are of concern to the industry as a whole because, of course, under-age people were having access to high strength alcoholic products.

**Senator BARTLETT**—Then there is also a major price advantage for those.

**Dr Muller**—Certainly, yes.

**Senator BARTLETT**—They are all imported, are they? Is that right?

**Dr Muller**—No. They are a mixture of imports and domestically reproduced goods.

**Mr Halmarick**—Usually what is termed ‘industrial alcohol’, so that is how they get away from paying any excise.

**Senator BARTLETT**—Right, industrial strength. Your submission in relation to the brandy-rum disparity is pretty clear cut, but in terms of some of the other tax treatments of alcohol that other aspect which will be, I presume, raised tomorrow—I was curious about its impact on your industry and the rum industry in particular—have you got any ideas, any figures on lost sales as a consequence of this type of product?

**Mr Halmarick**—No, I have not seen any specific lost sales. There would be some, but it would not be significant. I think it is more an issue of responsibility and lost revenue to the government and things of that nature, as far as the essences are concerned. They have got 75 per cent alcohol in a product that sells for \$4.50 in the shop—it is terrible.

**Senator BARTLETT**—I assume if that loophole is not addressed, then it is an area that could quickly grow—

**Mr Halmarick**—Absolutely, because more and more people would see the opportunity to boil up some sugar and water and add these essences and end up with so-called rum for very low costs.

**Dr Muller**—Some are also being sold through places like home brew shops as make-your-own spirits, so you can brew up a brew and toss in a bit of flavouring and you get a pretty potent mixture. That would be a direct competition which we would have concern about, although the volumes, I am sure, are not huge. But they have the potential to cause detriment to the image of the industry and that is something that we really do not want to see.

**Senator HARRADINE**—On the disparity between the excise treatment of brandy and rum, has it anything to do with the medicinal qualities of both or the lack thereof?

**Dr Muller**—It was originally brought in in the late seventies when there was a glut of wine grapes and it was an industry assistance measure originally.

**Senator HARRADINE**—But has that never been raised?

**Dr Muller**—It has never been raised, to my knowledge, senator, as a point in favour of a differential.

**Senator HARRADINE**—Which gives you the greatest headache—rum or brandy?

**Dr Muller**—I can assure you they are exactly the same. Alcohol is alcohol as far as headaches are concerned.

**Senator CONROY**—Can I clarify that what you are interested in doing is getting the two taxed at the same rate.

**Dr Muller**—Yes.

**Senator CONROY**—You do not have a preference of whether or not you go down to brandy or brandy comes up to you; just that they are at the same rate?

**Dr Muller**—We would prefer to go down to brandy.

**Senator CONROY**—But if the government was to put brandy up to your rate, then you would be happy?

**Dr Muller**—We would be less unhappy.

**Senator CONROY**—Frightened of your own success.

**Dr Muller**—Clearly it would be an advantage to domestic producers if the domestic spirits were treated in the same way and other spirits, which are 100 per cent imported, are treated differently. This is a legitimate way to do it. It is not a tariff means of protecting or giving assistance to an industry.

**CHAIR**—Let me ask a pointed question then: if it went down to brandy, would you pass the savings on to your consumers, or would you pocket it?

**Dr Muller**—Yes, we would pass it on.

**Mr Halmarick**—I think even with the government saying the ACCC would have a role to protect, make sure that no-one took advantage of any change—

**Senator CONROY**—Are you saying that with a smile on your face?

**Mr Halmarick**—No way, because that is it, and you would pass it on.

**Senator FERGUSON**—Can I say, firstly, I think it is unlikely that you will come down to brandy. I have not known many governments to reduce excises to that level. The point I am really making is that, apart from this particular issue of the disparity between brandy and rum, the Bundaberg Distilling Co. supports the tax reform package?

**Dr Muller**—Yes. Not in terms of the level of excise.

**Senator FERGUSON**—No, but the overall principle.

**Dr Muller**—The principle, absolutely.

**Mr Parlett**—As Senator Bartlett pointed out, Bundaberg Distilling Co. is a member of DSICA and they will be making representations tomorrow, so you can take it that Bundaberg supports the position of DSICA, apart from on this issue.

**CHAIR**—I think your position is pretty clear to us.

**Dr Muller**—There are some technical calculations of the rates which we would ask the senators to take to heart.

**Senator GIBSON**—Thank you, Chair. Mr Halmarick, you made reference to bourbon earlier on but I did not understand why.

**Mr Halmarick**—Bourbon is the major product, I suppose, which competes with rum.

**Senator GIBSON**—But there is the same excise on it, though, isn't there?

**Mr Halmarick**—Yes. However, some of the secondary bourbons, if you like, on the market today are being sold at a prime retail price less than Bundaberg.

**Senator GIBSON**—In spite of the same excise?

**Mr Halmarick**—Yes, because their costs of landing it here are a wee bit cheaper than the costs we have producing Bundaberg. I suppose in terms of some of the food standards which are significantly incorrect in Australia—inasmuch that you can sell some American whiskies in Australia as bourbon when you cannot sell them as bourbon in America, which allows cheap products to come in and be sold as bourbon—that is something hopefully the Australian and New Zealand Food Authority will address—

**Senator GIBSON**—Okay, a separate issue.

**Mr Halmarick**—although I am fearful of the initial results.

**Senator GIBSON**—Thank you for the explanation.

**Senator FERGUSON**—Can I ask a question that is not directly related to our terms of reference, but I did notice at a function you had in parliament house prior to Christmas that, in fact, you were promoting a product which contained Boags beer, I think, and Bundaberg rum. Could you tell us which product you were trying to improve?

**CHAIR**—I think you should take that on advisement. That is indeed a loaded question. We have a Tasmanian senator here. Just speaking for myself, reflecting as I gaze out the window, I hope we can have a unanimous recommendation on your submission. All of us seem to be now moving into indulging ourselves just a little. This is sheer self-indulgence, so I apologise up front. Why do you allow Mount Gay Rum to sponsor or be a part sponsor for the Sydney-Hobart yacht race? Why isn't Bundaberg on our hats?

**Mr Halmarick**—That is an interesting question. I happened to be down at the CYC the other day, and it seems to me that the supplier of most of the spirits to the bar, who happen to have the pouring contract, happens to be the distributor for Mount Gay, and I think that is how it happened. We have a lot of sponsorship with the yacht clubs in Victoria, Geelong, up at Hamilton Island and other places.

**Dr Muller**—There is actually a competition conducted in one of the bars in Hobart at the conclusion of the race which features Bundaberg rum very significantly.

**CHAIR**—I must have missed that. Thank you all for assisting the inquiry. We are now adjourned for afternoon tea.

**Proceedings suspended from 3.40 p.m. to 3.59 p.m.**

**GROVE, Mr Basil William, Committee Member, Australian Coalition for Economic Justice**

**MacDONALD, Mr Keith, Committee Member, Australian Coalition for Economic Justice**

**O'HALLORAN, Mr Brian Francis, Committee Member, Australian Coalition for Economic Justice**

**CHAIR**—Could I ask all of you gentlemen, as a group, which one of you is going to be the spokesman? Mr O'Halloran?

**Mr O'Halloran**—Yes.

**CHAIR**—Welcome on behalf of the Senate committee to this inquiry. Thank you for lodging a submission. Would you care to introduce your colleagues and then address us briefly on what you have put in writing so that we can then, if we may, ask you some questions.

**Mr O'Halloran**—My colleagues are Keith MacDonald and Basil Grove. We are founding members of the Coalition for Economic Justice. Basil will be referring to particularly small business. He is a small businessman himself. Keith's particular area of expertise is reading the Reserve Bank reports and applying them to where society is at. With regard to our presentation, I thought that we might specifically address three points: the first point relates to the impact of GST in relation to the five million plus Australians who live below or near the poverty line, and that is our major concern in fact. There are two other points we feel are terribly relevant also and they are part of our presentation. One of them is the question of the mandate itself in terms of its validity. The third is that we do have a proposal that might result in a more authentic mandate and tax system.

Very briefly, I would like to mention my own background. Prior to my fairly recent retirement I was the Executive Officer for the Catholic Justice and Peace Commission here in this diocese and for 10 years I operated in that capacity. During my tenure in that capacity, in 1992 the Australian Catholic bishops produced a document based on an inquiry into the distribution of wealth in Australia. After 1,300 submissions and hearings, the document came down and was identified or named *Common wealth for the common good*. There is some concern, in terms of our presentation, from information that was produced through that document because we feel it does have relevance here.

Also there is some reference we would like to make to the fact that in 1992 the bishops' document drew on this fact and the United Nations Human Development Commission produced a document identifying that over a period of 30 years the wealth of the top 20 per cent of the world's population had changed from 30 to one—30 years prior—to then, in 1992, 150 to one. So the whole development of wealth appeared to be moving very dramatically up the ladder, not across the board. Similarly, the document from the bishops' inquiry found itself—even though it had started to look at the distribution of wealth—particularly concerned because of the gravity in the growth of poverty in Australia.

As well as having been involved at that level, I also went to Canada in 1995, addressing the issues of particularly GST itself, and in 1997 to New Zealand. So there is some background experience there. It is from that background that I press on with regard to our major concern, namely the impact of the GST on the disadvantaged. The questions that we ask ourselves and we feel are relevant to this inquiry are: what does the function of the GST, or the tax system, or taxation, need to be in terms of the distribution of wealth? What will be the relevance of GST in relation to the five million plus Australians who are living below or near the poverty line? We feel that is a very grave question and we feel we have not been provided with any information to this stage that would indicate that the GST will in any way whatsoever make a contribution towards the alleviation of poverty.

We are also concerned about the fact that income tax—which is a vehicle of wealth distribution—is being reduced by \$13 billion. The question is: how relevant is that to, once again, the five million disadvantaged Australians? We have a graph that is drawn on the figures provided by the Treasury identifying what the advantage is from the income of \$20,000 a year up to \$150,000. In some regards the obvious commitment and direction of that strategy is not towards the five million but, to a very large extent, to the advantage of those probably least needing the advantage.

We are also concerned about the service tax and how it is going to impact on the people least able to carry the burden. Just even at a personal level, in my own street within the last couple of days I have encountered an aged couple living in their own home and they have just been advised by the plumber that they are going to have to have their drainage replaced because over the years there has been an inundation of tree roots. The figure there is \$2,200 that they are going to have to provide. If that happens before GST or after, there is a significant difference again. There are people who are living on a day-to-day basis, dollar for dollar, and unexpectedly the family car breaks down, or the house is due for repainting or things like that. How relevant is the GST in terms of at least trying to ensure alleviation of poverty, rather than increasing it?

Another thing is: how many institutions serving those in need cope? The information that appears to be coming out of this very inquiry is disconcerting. We see the Australian Catholic Health Commission has had a study done by an independent source identifying that over three years it will cost \$153 million to just that one particular group. If you spread that right across the broad service deliverers for the disadvantaged, what will the impact be? We also are concerned about the impact on small business because there has been tremendous growth of poverty among people in small business. This has been reflected in many ways, even, tragically, in a massive increase in the number of suicides in Australia.

Finally, our concern is very much, will GST become the focus of concern of government? Will the area of concern which we think should be most focused upon—namely that of the culture of avoidance and evasion—become even less important than it is today? They are the points that are of concern to us specifically in regard to our submission. Keith, you might like to make some reference to how that graph works.

**Mr MacDonald**—Mr Chairman, we were very interested in these figures published in the *Financial Review* of 14 August last year. They were supplied by Treasury and headed,

‘What do you get from tax reform? Weekly cash gain from reform after GST and inflation effect’.

We took as our base income \$20,000 a year, and the weekly cash gain, according to the figures published, was \$4.28. We took that as the base rate. As the incomes increased the weekly cash gain did not go up proportionally, but it increased much more rapidly. For instance, on a \$40,000 income per annum, which is twice the base income, the weekly cash gain was \$16.66, which was 3.89 times the basic rate. For \$50,000, which was 2½ times the base income, the weekly cash gain was \$39.60, and the ratio to the base rate was 9.25. So for a 2½ times increase in the base income, the increase in the weekly gain was 9¼. At \$60,000, which is three times the base income, the cash gain was \$51.18, which was 11.96 times the base rate. So for a three times base income we had nearly 12 times the base rate.

For \$70,000, 3½ times the base income, the weekly cash gain was \$62.76, which is 14.66 times the base rate. So for a 3½ times increase in the income, the increase in the weekly cash gain was 14½ times. At \$80,000, which is four times the base income, the weekly cash gain was \$67.62, which is 15.8 times the base rate, so we had an increase of four times in the base income but an increase of nearly 60 times in the weekly cash gain. At \$90,000, that is, 4½ times the base income, the weekly cash gain fell off slightly to \$65.78, which was still 15.37 times the base rate. So for a 4½ times increase in the income, the increase in the weekly cash gain was more than 15 times. For \$100,000, five times the base income, the weekly cash gain was \$63.93, and the ratio to the base rate was 14.94. So for five times the base income we had nearly 15 times the weekly cash gain.

That is just a sample of those figures and they illustrate our point. If you would like a copy of these, I have a few to spare.

**CHAIR**—If are given to the officer, he will photocopy them for the committee. I assume it is your intention to add this to your written submission?

**Mr MacDonald**—Yes.

**CHAIR**—We will include it.

**Mr MacDonald**—Basil, possibly you might like to make some reference to the small business sector.

**Mr Grove**—Yes. I am particularly concerned about the effect that it will have on small business, as that is where I make my living, especially in areas that do not seem to have attracted any attention. For example, I have seen a film clip of Senator O’Chee criticising the two per cent easy tax that was promoted by One Nation. Now, I certainly do not wish to defend either One Nation or the two per cent easy tax, but the ground of criticism which Senator O’Chee used was that it would advantage big business at the cost of small business, but if you consider the effect of the GST then the same thing must occur. Yes, I beg to differ! There are plenty of instances where that can be shown to be the effect that will come out of it.

In particular, if you consider the example of the large retailers, the large retailers buy on credit and sell for cash, and if you consider their position at the starting point of the introduction of a new tax, they will have on their shelves a large amount of stock which has not been paid for, but they will be collecting GST on it. For whatever the holding period of the tax before it has to be submitted and reported, they will have the benefit of having that tax in their bank account.

For the small business it works in almost exactly the opposite way, because very few small businesses—perhaps some in the retail game—are in a position where they are holding stock at no cost to themselves. They are holding it at considerable cost to themselves, so they are in a very weak negotiating position with their suppliers and their customers. So they will be in fact holding goods on their shelves which shall have cost them 10 per cent more. Of course, at some time down the line they will be collecting tax receipts which will tend to lower the burden; but there will still be an increase in holding costs for small businesses which are in a weak position vis-a-vis their suppliers and their customers in their credit relations, as opposed to large business, which has the whip hand.

There is another effect that comes out of it which has been given no attention whatsoever, and it was illustrated very nicely for me just this afternoon by a gentleman who is a reporter in the court here. There are several small newspapers in Toowoomba who use the services of a typesetting company, and they do this because it is clearly efficient for them all to do that rather than have those services in-house. When a tax of the nature of the GST is introduced, those services shall cost those companies 10 per cent more. Because they are selling direct to the public, they will have no alternative but to pass that on. That militates against efficiency. Do you believe the effect is not what I say it is?

**Senator FERGUSON**—Only that if it is a cost of business of course it will be rebated so it will not cost them 10 per cent more.

**Mr Grove**—They have to pass it on to the final customer.

**Senator FERGUSON**—No, because they get it rebated in full.

**CHAIR**—They have to pass it on and then claim it back.

**Senator FERGUSON**—They do not pass it on to the consumer.

**CHAIR**—They impose 10 per cent on their product, sell their product, obtain the 10 per cent and, at a quarterly interval, claim it back.

**Senator FERGUSON**—So it does not cost them 10 per cent more.

**Senator O'CHEE**—In fact, it is cash flow positive.

**Mr Grove**—Well, in that particular case, yes, I would concede that, I am sorry.

**CHAIR**—That is at one end of the process. Of course, at the other end, when they are buying inputs they have to pay 10 per cent on those.

**Senator FERGUSON**—So you asked us why we were shaking our heads, and that was why.

**Mr Grove**—Okay. Thank you. Well, I still believe that there are a number of instances where big business, although they are obviously complex situations, will have less trouble with the GST than small business will. They will certainly have less trouble in the fact that they have accounting systems over which the cost of their operation can be more readily spread than a small business person who has to do an increased paperwork load for a relatively small amount of money and for a relatively small operation.

**CHAIR**—Thank you. Mr O'Halloran, is that your presentation?

**Mr O'Halloran**—Yes.

**CHAIR**—Good. You are now available for questions?

**Mr O'Halloran**—We are.

**CHAIR**—Okay. If I can ask, what are you actually asking us as representatives of the Senate to do? From your presentation I make this assumption: are you asking us to not support the government's tax legislation, or are you asking us to amend it in some way?

**Mr O'Halloran**—What we would ideally like to see is a situation where the whole idea of the validity of mandate be looked at because, even in the light of the experience of this Senate inquiry, reading the daily papers and attempting to keep pace with the issues that have come out, I cannot see how the Australian people could have been called upon to provide a mandate with the lack of information; information that should have been available and is essential if we are going to fulfil our commitment in terms of rights and the democratic process. That is our concern: namely, the validity of the mandate itself when it has the potential to represent such a dramatic impact on the lives of so many people and with so much uncertainty in terms of the destiny of this nation anyway. That is one area of concern.

Our proposal is that the fruits of this inquiry be used to provide a referendum, or be the process that would act towards establishing an authentic mandate. That authenticity should come from information, participation and being given enough time to ensure that the electorate is educated. On that basis I think we could honestly say that might be an authentic mandate. But it should also be done, we believe, in the context of using the fruits of this inquiry to identify the pros and cons of the GST but also to open up alternatives to a GST. A GST is not the only option and, surely, at this particular stage in our history—moving into the 21st century—rather than rush in with so much uncertainty about impact and ensuing results, we should commit ourselves to a process that will guarantee that the citizens of tomorrow, and many tomorrows, at least are going to live under a model that is ideally a witness to a commitment to social justice and the common good. To do that, I believe, would require a tremendous process.

**CHAIR**—I understand from what you are saying that, firstly, you question the authority of the government to proceed down this course on the basis of having a mandate. That part is clear. The second part is that you think this is a wrong-headed approach and that there ought to have been a canvassing of several options, some with a GST, some without, so that there was a greater understanding of the types of variations you could make in a tax system.

From your earlier submission, am I also right in believing that an acceptable outcome in tax changes for you would be one that made sure there was a redistribution of income from the wealthy to the poor in order to sustain them more effectively? Do I understand that to be the case?

**Mr O'Halloran**—Not in the context of charity, though.

**CHAIR**—No.

**Mr O'Halloran**—But rather in the context of interdependence.

**CHAIR**—Finally, this is all wrapped up in a bundle of saying to us, as the Senate, how we reflect your view to our colleagues in the Senate. Do I understand that until this is done you are not in favour of our passing the bills that are before us?

**Mr O'Halloran**—Yes.

**Senator FERGUSON**—How many members does your organisation, ACEJ, have?

**Mr O'Halloran**—It is not an individual membership organisation. We have about 40 organisations and they range across the spectrum, including church groups. We deliberately do not have political parties as part of the coalition, but we have members of parties, naturally, who are part of it.

**Senator FERGUSON**—It is just that I am looking at the bottom of your submission where you talk about having a variety of sectors, including trade unions. But I presume you have only got some individuals from trade unions. You have got churches—

**Mr O'Halloran**—No, there are some actual unions.

**Senator FERGUSON**—Unions that belong in total?

**Mr O'Halloran**—Yes, as unions. Also, the National Federation of Independent Business is part of the coalition. That is an interesting thing because the trade union movement and small business are finding themselves more and more victims of what some would say are the processes of globalisation and economic rationalism. Australian Pensioners and Superannuants are part of the organisation.

**Senator FERGUSON**—How do you make the link between economic rationalism and tax reform?

**Mr O'Halloran**—Both of them impact very dramatically on the lives of people. Under the heading of 'economic rationalism' we would look at the planks of privatisation—and that is not to say we are opposed to all forms of privatisation.

**Senator FERGUSON**—But that is not part of the tax reform package.

**Mr O'Halloran**—No, the interrelationship is between—

**Senator FERGUSON**—There is no interrelationship. We are a select committee looking into a new tax system and there is no relationship between economic rationalisation or privatisation and the tax reform system.

**Mr O'Halloran**—No, I was answering your question in relation to what organisations go to make up the coalition. I was not answering it in the context of its being a proposal on behalf of this organisation towards an income tax plan.

**Senator FERGUSON**—I think almost all of the OECD countries, many of whom have left-wing or socialist governments, have had a VAT introduced by their governments. Why do you think so many of those countries use a value added tax or a goods and services tax to underpin their economy, and particularly their social welfare system which, in many of those countries, some would consider is a very generous social welfare system?

**CHAIR**—Which ones have left-wing and socialist governments? You said OECD countries. Which ones are they?

**Senator FERGUSON**—I said when it was introduced. Even New Zealand had a socialist government when they introduced it.

**CHAIR**—They had a Labour government.

**Mr O'Halloran**—They had a Labour government, absolutely.

**Mr Grove**—Far and away the most successful country in economic terms in the OECD does not have a value added tax and it probably has a greater GDP than all the others put together. I think that is significant too.

**Senator FERGUSON**—Are you referring to the United States?

**Mr Grove**—Yes.

**Senator FERGUSON**—In fact, they do have a goods and services tax.

**Mr Grove**—They have state sales tax.

**Senator FERGUSON**—It is a state based goods and services tax.

**Senator SHERRY**—No, it is not a goods and services tax.

**Senator FERGUSON**—It is.

**Senator SHERRY**—No, it is not. It is a retail tax, with different rates in different states.

**CHAIR**—We will not debate it here anyway.

**Senator FERGUSON**—I will not debate it with Senator Sherry here.

**Mr O'Halloran**—I cannot answer your question but I have a few ideas about it. I think we could ask that same question about many things regarding privatisation. Some people who were in favour of it are now saying it is the wrong way to go. We are seeing more and more economists claiming that maybe we got it wrong. As a matter of fact, next month the former Deputy Prime Minister of Canada will be in Australia. He is an author, and virtually his whole journey to date seems to be attacking the whole model that has become the dominant global model. He virtually uses those terms: 'We're going the wrong way.'

**Senator FERGUSON**—Most people agree that Canada went the wrong way. Can I just ask another question on a different issue which Mr Grove raised, and that is the issue of small business. Are you a member of a small business association at all, Mr Grove?

**Mr Grove**—No, I am not.

**Senator FERGUSON**—For any particular reason?

**Mr Grove**—No, for no particular reason.

**Senator FERGUSON**—It is just that your position is at odds with all of the organisations of small business that have submitted any evidence to us, or that we have talked to, because they are very supportive of the tax reform proposals. COSBOA and all the major small business associations are actually in favour of the tax reform package.

**Mr Grove**—That may well be the case for the organisations, but I suspect that if you went out into the street and actually spoke to the small business people themselves, and if they actually had been fully apprised of what is involved, they might disagree. On what grounds do these organisations submit that it is favourable for them?

**Senator FERGUSON**—Because they have asked their members specifically—

**Mr Grove**—But on what specific grounds? Why are they saying, 'This is good for us'? They are suddenly going to be landed with a whole lot of extra work and become tax reporters for the government—

**Senator FERGUSON**—But what are they now?

**Mr Grove**—Why are they saying it and on what specific grounds? What is it about the package that they say is good for them?

**Senator FERGUSON**—Practically everything.

**Senator SHERRY**—Don't let yourself be verballed.

**Senator FERGUSON**—Well, I was asked the question by the witness, which is a pretty unusual way of going about an inquiry.

You talk about the extra paperwork, et cetera, for people who have experienced a goods and services tax in New Zealand, which the economics committee—not this committee—specifically went to see. The average small businessmen said it took them 10 minutes every two months to do their paperwork, so they did not consider it to be a burden.

**Mr Grove**—I find that unimaginable. If anybody who is making any number of sales in a month, has to tot up the amounts of those sales, the value of the tax put on them and then the amount of tax on the purchases and then sort all of that into two columns, can do it in 10 minutes then they have a really wonderful—

**Senator FERGUSON**—Don't you keep those records now?

**Mr Grove**—Of course I do, yes. I do them manually; I do not have a computer, because I am a genuine small business man.

**Senator FERGUSON**—I understand that.

**Mr Grove**—I am a self-employed individual, and I do not believe that anyone can do three months of reporting in 10 minutes in any system.

**Senator O'CHEE**—We are only asking for your total sales and total purchases in three months. We are not asking for individual ones.

**Mr Grove**—Yes, but they have to be added up. Somebody has got to sit down there and go through all of these purchases that you have made which have been taxable, take the tax component out of them, total it all up and then add up all your sales and do the same thing for those. If you are making any number of sales, this is not something that I think you can do in 10 minutes, and a lot of it is where there would probably be doubtful amounts to be apportioned. Some things in a purchase might be deductible and some might not be as a business input, and so on.

**Mr O'Halloran**—Regarding your comment, the National Federation of Independent Business is totally opposed to GST.

**Senator FERGUSON**—Can I say that I have never heard of the National Federation of Independent Business. To the best of my knowledge they have not put a submission in to the inquiry either. Are they a local organisation?

**Mr O'Halloran**—They would be the highest profile in Queensland of the small business organisations. They have been having an ongoing battle, attempting to get some sort of equality in the retail industry, seeing themselves as very much the victims of deregulation favouring 'the big three'. It is not an insignificant organisation.

**Senator FERGUSON**—I think I had better concede to somebody else, Senator Cook, because I am conscious of the time.

**CHAIR**—Thank you, Senator Ferguson.

**Senator BARTLETT**—I note your general principles that you put here in terms of a progressive taxation system and those sorts of principles. Do you believe that any form of taxation of services is automatically regressive?

**Mr MacDonald**—I would say it certainly is regressive. I think the services tax is a most iniquitous tax. I had an experience myself a few years ago of having to make repairs to my house and altogether they cost \$5,000. The 10 per cent on top of that would be another \$500 and I would not get that back in any rebate of income tax because I do not pay any income tax. I do not make the grade really. As a pensioner I do not pay any income tax if my income is less than about \$11,000 a year. So that would have been an extra tax of \$500, and since a lot of pensioners and retirees live in old houses, the maintenance of them costs them plenty over the years, as Mr O'Halloran was just saying.

Professional people charge fairly well for their services; that we should have to pay a tax on their income seems to me quite iniquitous. I think it is much fairer if they pay tax on their own incomes instead of leaving the victims to do it—if I may call them that.

**Senator BARTLETT**—Are you broadly aware of what ACOSS has been putting forward in their proposals for taxation reform?

**Mr O'Halloran**—Broadly.

**Senator BARTLETT**—Have you got any comment in terms of your views about the thrust of what they are proposing; whether you think they are on the right track or not?

**Mr O'Halloran**—I feel that in terms of their suggestion that we should be looking to recoup tax from avoidance, in those areas, it would be a question of straight-out justice and the function of government.

**Senator BARTLETT**—In terms of some of the other areas they have talked about, they make a point similar to yours in relation to compensation which you have mentioned in your submission. One of the aspects—not the only one—that they put forward to address that is to exempt food from GST as a major component that impacts on overall price increases. Would that be a position you would support?

**Mr O'Halloran**—We do not favour it. GST can be the distraction from ultimately establishing what we would call a just tax system. For instance, I have a document here that refers to the fact that, out of 7,760 transnationals last year, 4,300 did not pay one cent of tax. So if we start to diminish income tax through to billion dollar give-aways and make our focus a GST, that is drawing into a tax net people who have lived out their tax contribution life and also the victims, the social victims—the unemployed and so forth. If that becomes the major focus of revenue raising, I feel it just reinforces the concept of, 'Whatever you can get away with, good luck.'

**Senator BARTLETT**—From our perspective as a committee that has to look at what the government is presenting us with, rather than necessarily putting forward our own proposed tax system from scratch, one of the issues that has come up a lot in the various committees has been that under the new tax system there will be a shift in the tax mix towards more indirect taxes, fewer income taxes, as part of the total tax mix. The point you made about tightening loopholes has come up a lot. Do you believe, in terms of the existing tax system, that the overall mix between direct tax and indirect tax is about right, or do you believe it should be tilted further in one way or the other?

**Mr O'Halloran**—I do not think it could be regarded as right in any way, shape or form when you have some people not paying any tax at all—businesses or firms not paying tax at all—and at the same time earning very generously, be it through income or whatever. I know there is a point of view around that of, 'I'm a self-made man. I did it my way and I deserve every dollar I've made,' but it totally ignores the fact that—be it Woolworths' chief executive who might be on a million plus a year or not—there happens to be a third almost of this population not far removed from the poverty line who are consumers, who contribute to the wealth of these very successful companies.

**Senator BARTLETT**—Do you believe that if we were to spend more energy targeting loopholes and unpaid tax or companies or individuals not paying their fair share—whether it is through loopholes or whatever—that form of tax reform would necessarily assist lower income earners as well?

**Mr O'Halloran**—It should assist. It must increase revenue, because it is revenue that has not been received now.

**Senator BARTLETT**—One of the arguments that is often put forward for the need for tax reform is to broaden the tax base; similarly, to provide the opportunity for more revenue, and to tax sectors of the economy that are not taxed at the moment. I accept what you are saying about the need to plug loopholes, et cetera, and dealing high income earners or companies that are not paying tax. I think that is an area that is appropriate to target. That does not necessarily mean that is not appropriate to also do other things.

**Mr O'Halloran**—Not necessarily at all, but one would imagine that the most urgent thing is to at least plug the leak. That is a starting point. Because it virtually is courting injustice. We are looking at a reform tax that could well be imposing a very heavy yoke on the shoulders of people least able to bear it. And at the same time we learn that there are many people not paying tax. We are not proposing a witch-hunt to charge around and try and extract every dollar out of every person who is earning well. The idea is that tax should be apportioned according to capacity to pay; no more, no less.

**Senator BARTLETT**—Sure.

**Mr O'Halloran**—If a person has the capacity to pay \$5 a week, that is it. If a person has the capacity to pay \$5,000 a week, well, that is it.

**Senator BARTLETT**—Yes.

**Mr O'Halloran**—But it is nothing more than the capacity to pay.

**Senator BARTLETT**—I am just trying to get an overall sense of the thrust of what you are suggesting we should be considering and recommending, again given that we have been presented with a proposal from the government to consider. I am just wanting to reflect it back to make sure I am getting the sense right. You are saying, basically, that we should really be focusing a lot more on plugging existing gaps and loopholes, targeting high income earners or companies not paying their fair share—going in that direction—rather than the direction that this package is going in. Is that basically right?

**Mr O'Halloran**—At this stage the priority, we believe, should be doing that, and setting in train a process that enables the Australian people to effectively arrive at conclusions. Surely a new tax system should be the decision of the people? We have not got an effective democratic process for that at the moment, with a deadline at the end of June and a Senate inquiry in place—that has not been part of the government's program—to try and sort this out. By rights, I think we should be putting a couple of years into this debate, into correct modelling, into identifying who the victims are and who the winners are, identifying the most effective processes to establish the common good so that there are winners. But that is not going to happen by rushing legislation through on the basis of a questionable mandate with a deadline of a few weeks.

**Senator SHERRY**—Just by way of introductory comment, we had two small business organisations appear before us in Adelaide last week. I cannot recall their names. One argued critically against the GST because of the impact on small business, particularly the administrative costs. Another argued for a GST but acknowledged that those small business operators—at least 50 per cent—who were not in the wholesale sales tax system faced an increased compliance burden because of the administration of a GST. So I think you are quite right in your observations, Mr Grove. What small business have you been involved in?

**Mr Grove**—I am a small manufacturer, and I am in the position that probably several hundred thousand Australians will find themselves in after 30 June next year if this goes through, and that is that we have, say for example's sake, a motor vehicle which is used partly for business and partly for private and we have a home phone which is, again, partly business and partly private, and we buy quite a number of business inputs and things like that in the form of, say, small stationery. That is probably taking it a little bit far, but you can see the point that when you are working from home with a small business it is not very easy to draw the line about what is a business input and what is a home input, in many cases.

Now, we are supposed suddenly to be able to produce a return every three months which splits all this up neatly and deducts one from the other, and do it in 10 minutes. I think that is just a bit of fiction, actually.

**Senator SHERRY**—You do not have a computerised accounting system?

**Mr Grove**—No, I do not. It is simply not justified because I do not have enough trade to justify that.

**Senator SHERRY**—Do you have any knowledge of other small businesses who run computerised accounting systems?

**Mr Grove**—I do, of course. I have acquaintances and customers and so on who have computers. I really do not know how much work will be entailed if they are using a computer. I simply have no understanding of that.

**Senator SHERRY**—But it will be extra work, won't it?

**Mr Grove**—Well, obviously more, but how much of course I cannot assess.

**Senator SHERRY**—Yes. Mr O'Halloran, in your submission you say the value of compensation can be eroded. I take it from that statement that you do not support a GST.

**Mr O'Halloran**—No.

**Senator SHERRY**—You see that not having a GST is the only effective way of ensuring that the relative position of the less well off in our society can be at least protected to some extent.

**Mr O'Halloran**—Yes.

**Senator SHERRY**—What do you think of the argument that ACOSS has, I will use the term, 'fallen for' that we need a GST to secure the government revenue base in order to provide increased funding for social security at a time when social security has been cut back?

**Mr O'Halloran**—I think that is terribly naive because it is a question of commitment. If governments are aware of the transfer of wealth away from ordinary, mainly low income people, and they are aware of the burdens that this creates on society, and can then turn a blind eye completely to the fact that we have 4,000 transnationals who pay no tax, and the trusts that are used to avoid tax also, and can then justify ignoring that on the grounds of: 'But if we do this other thing, which could possibly'—and I believe probably—'hurt many more people, well, at least we will be able to give you a little bit more money to look after them with,' it just does not ring true.

**Senator SHERRY**—Just referring to the schedule that you attached to the paper you presented today, the *Financial Review* document, I take it you do not regard it as fair—and this is but one example—that a single person who earns \$20,000 gets a cut in income tax of \$4.28 or 1.3 per cent per week, versus a person who earns \$75,000 who gets an income tax cut of \$68.55 a week or, more importantly, a 7.3 per cent cut, which is about six times in percentage terms, not money terms, what a person on \$20,000 will get. I take it you do not regard that as being a fair proportion of the income tax cuts?

**Mr O'Halloran**—It comes down to responding to need as a priority, doesn't it, and it does not seem to be happening very well there, particularly at a time when we are hearing governments justifying GST on the grounds that they need more money to give to the disadvantaged.

**Senator HARRADINE**—This is a total package. There are other things other than the GST in it. I understand the points that you are making about reduction in poverty and so on. You would agree, however, that families with children by and large are grossly overtaxed for a number of reasons, including bracket creep?

**Mr O'Halloran**—Yes.

**Senator HARRADINE**—You will have noticed that page 188 of this document sets out the situation of the one-income couple with three children, one aged under five. For that one-income family on \$30,000—which is not a dreadfully enormous amount for a family to exist on, for example, in Sydney—their current tax liability is \$121.71 a week. Now, what should be done about that? Shouldn't that family get a better go than that sort of thing? They should not be paying that sort of money in tax, surely?

**Mr O'Halloran**—No.

**Senator HARRADINE**—What is your proposal for those people?

**Mr O'Halloran**—Once again, somehow or other we have to increase the slice of the cake, but not by imposing a greater burden on those least able to carry it. But surely those people are entitled to a tax that they are capable of paying?

**Senator HARRADINE**—I understand. So your reference to capacity to pay included the issue of the number of children the family has—

**Mr O'Halloran**—Yes, all the necessities.

**Senator HARRADINE**—the capacity to pay vis-a-vis others on the same income level, and you take into account, of course, the size of the family.

**Mr O'Halloran**—The necessities to exist, to live with dignity as a family.

**Senator HARRADINE**—I am going to the question of tax equity now. Is it fair that a family with, say, four children on a particular income level should be taxed at the same rate as a single income earner on the basis of horizontal tax equity? You would agree that on the basis of horizontal tax justice or equity it would be unfair to tax, at whatever level of income, a family with five children at the same rate as a person with no children?

**Mr O'Halloran**—I think the idea of capacity to pay accommodates that very thing. If you have four children you naturally have less capacity to be taxed than if you are a single income earner on the same income figure.

**Senator HARRADINE**—You appear to be against the tax package itself, particularly the GST area. What is your view of the GST application to everything else barring food?

**Mr O'Halloran**—We are opposed to the GST totally, and it would be regrettable that by exempting food it was able to pass, because it still carries with it, we believe, very unfair burdens that would be primarily imposed on those least able to carry them.

**Senator HARRADINE**—Are you aware that other necessities of life such as clothing, payment of utilities such as gas and electricity, et cetera, transport costs and rents add up to almost 40 per cent of the expenditure of the lower income groups that you were talking about? Food I think is something like 23 per cent from memory. So are you saying that the package should not proceed even if food were exempt?

**Mr O'Halloran**—Correct.

**CHAIR**—No further questions? I think we are right on time. Can I thank you for appearing before us today and helping us with our inquiry, Messrs O'Halloran, MacDonald and Grove. This committee is now adjourned until 9.00 a.m. tomorrow.

**Committee adjourned at 4.56 p.m.**

