

# Pre-Budget Submission

2007-08

NOVEMBER 2006



**CPA**  
AUSTRALIA



# Introduction

CPA Australia, the pre-eminent body representing the diverse interests of more than 108,000 finance, accounting and business advisory professionals working in the public sector, public practice, industry and commerce, academe and the not-for-profit sector, is pleased to make this 2007-08 Pre-Budget Submission.

The following areas are of priority to our members, their clients, and the accounting profession and submitted in the public interest. Our submission is driven through input from our membership, business committees and policy centres of excellence/research think-tanks.

We look forward to the opportunity to discuss these areas and the following recommendations further with the Federal Government and Treasury. Please contact our Manager of Government Relations, Ms Liz Lang in Canberra on (02) 6267 8544 or [liz.lang@cpaustralia.com.au](mailto:liz.lang@cpaustralia.com.au) for further information.

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# Recommendations

## 1.0 Taxation

### 1.1 Personal tax reform

- Further reform is required in the area of personal income tax to ensure that the system remains fair, efficient, and internationally competitive.

### 1.2 Business tax reform

The Government should implement the Board of Taxation's earlier recommendations to:

- Provide a 20 per cent tax credit to shareholders on unfranked dividends paid out of foreign source income.
- Allow dividend streaming of foreign source income.

### 1.3 State and territory tax reform

- CPA Australia would like to see further reforms of the remaining inefficient state/territory taxes addressed by the Commonwealth and states through the COAG process.

### 1.4 Statutory privilege for clients of non-legal tax advisers

- CPA Australia recommends that the Government considers the introduction of a statutory privilege for accountants similar to legal professional privilege as adopted in New Zealand.

### 1.5 Volunteers and deductible gift recipients

In recognition of the contribution of volunteers to communities around Australia, CPA Australia recommends:

- The Government makes a tax exempt annual payment to volunteers.
- Alternatively, volunteers who make a contribution to deductible gift recipients be allowed a rebate or deduction for certain costs incurred (such as travel, uniforms etc) in respect of these activities.

## 2.0 Superannuation reform

CPA Australia puts forward the following superannuation recommendations:

### 2.1 Extend deductibility of superannuation contributions

- Abolish the '10% rule' for the deductibility of superannuation contributions to provide greater incentive and flexibility for people who have to make their own superannuation provisions.

### 2.2 Default scheme for voluntary personal contributions

- Introduce a 3% voluntary superannuation contribution scheme.

### 2.3 Superannuation guarantee threshold

- CPA Australia recommends the SG threshold of \$450 per month be abolished so as to boost retirement savings, particularly for people with broken or casual work patterns.

### 2.4 Superannuation simplification

- CPA Australia recommends all superannuation death benefits should be tax free after 30 June 2007 not just those to dependants.
- To further remove the incentive for these schemes and arbitrage, CPA Australia recommends that the current inconsistencies between the definitions of 'dependant' in the SIS Act and the Income Tax Assessment Act 1936 be removed by aligning the definition of child in the ITAA 1936 with that in the SIS Act.

### 2.5 Commutation of existing complying pensions

- Commutation of existing complying income stream to be permitted from 20 September 2007.

### 2.6 Concessional contribution limits

- The transitional period for the cap on concessional contributions for over 50s to be extended to 10 years.

### 2.7 Overseas benefits excluded from contribution limits

- Transfers from overseas superannuation funds should be excluded from the contribution limits.

### **3.0 Skills shortage and workforce participation**

To alleviate the shortage of professional accountants, CPA Australia would like to see an integrated program of support which includes:

- Increased emphasis on English language skills and work experience when assessing skilled migration visa applications.
- Stronger requirements for universities to provide English language training for international students.
- Provision of funding to universities to incorporate work experience placements for accounting students.
- Additional support for skilled migrants to develop English language proficiency and work experience once they leave university.
- Encouragement for universities to allocate more HECS places to accounting-based disciplines
- Increase in the overall number of domestic accounting HECS funded places.
- Coordinated national strategy to debunk negative perceptions about older employees.

# 1.0 Taxation reform

## 1.1 Personal tax reform

Given Australia's strong reliance on personal taxes as a source of revenue, continued personal tax reform is necessary to ensure the personal tax system is fair, efficient and internationally competitive. The system also needs to be structured so it can adequately meet future government spending requirements including those arising from the ageing population.

CPA Australia acknowledges the reduction in personal taxes through a combination of threshold and rate changes since the inception of the New Tax System (NTS) in mid-2000. The changes implemented from 1 July 2006 are an important step in providing greater incentives for higher levels of workforce participation as well as providing tax relief and enhancing competitiveness.

Notwithstanding these changes, CPA Australia believes more needs to be done to fully modernise Australia's tax and transfer systems, primarily focusing on revenue neutrality, the distributional impact of reform and effective marginal tax rates (EMTR).

Effective tax reform in Australia will bring about a more efficient and productive economy through removing some of the key disincentives to saving and investment and participation in the workforce, especially by second income earners in a family. CPA Australia notes in this regard that Australia has one of the lowest participation rates by second income earners of any of the OECD countries. This is partly explained by the EMTR problem.

Recent modelling done for CPA Australia by Atax – University of New South Wales, as part of an Australian Research Council (ARC) project, indicates that significant reform of Australia's personal tax system can be achieved on a broadly revenue neutral basis and is consistent with the criteria discussed above.

Further details of one such possible reform for the 2007/08 income year and beyond, and the associated revenue implications are contained in the following two tables:

### Financial Year 2007-2008

Taxable Income	Marginal tax rate (MTR) (%)
\$0	13
\$6,000	13
\$26,000	26
\$75,000	38
Low income rebate	\$900 for income < \$26,000 per annum
CGT discount	Remove CGT Discount, exempt for the first \$5,000 per annum
WRDs	Remove all work-related deductions, give back \$400 to taxpayers who claim WRDs

### Revenue Impacts

	\$million
Government loses from change in tax rates and thresholds	-\$4,168.42
Government gains from removing CGT discount	\$4,107.64
Government gains from removing WRDs	\$3,650.99
Loss from \$300 pay back (tax rebate)	-\$3,646.71
<b>Final Impacts: Government gains</b>	<b>-\$56.50</b>

This preliminary modelling suggests there are no significant adverse revenue implications nor distributional impacts arising from such reforms. CPA Australia's work in this area is ongoing and it will publish the results of the project in the first half of 2007.

### Recommendation

- Further reform is required in the area of personal income tax to ensure the system remains fair, efficient, and internationally competitive.

## 1.2 Business tax reform

One issue remaining as a limitation on Australian business is the continuing double taxation of offshore profits in the hands of Australian investors. While the profits of foreign subsidiaries and branches of Australian companies are now generally exempt from company tax, they continue to be taxable when distributed to shareholders even if those profits have already been subject to a level of taxation in the foreign jurisdiction.

Companies need the ability to frank their foreign income to avoid this double tax bias. Currently, the dividend imputation system gives companies franking credits only in relation to dividends from domestic business activities.

The Review of Business Tax (RBT) in 1999 and the Board of Taxation (BoT) in 2003 both identified the need for a level playing field in this area. The BoT recommended the Government provide a 20 per cent tax credit to shareholders on unfranked dividends paid out of foreign source income and allow dividend streaming of foreign source income. However, neither of these changes have yet been adopted.

This issue is important for major listed public companies as international expansion imposes pressure on their ability to pay fully franked dividends that are typically preferred by share market investors. It is also a problem for many privately owned companies who are less likely to be able to retain profits as those profits are increasingly derived from foreign operations.

Accordingly, CPA Australia believes the Government should implement the BoT's earlier recommendations on this matter to ensure that Australia remains an attractive location for companies growing offshore.

### Recommendations

The Government should implement the BoT's earlier recommendations to:

- Provide a 20 per cent tax credit to shareholders on unfranked dividends paid out of foreign source income.
- Allow dividend streaming of foreign source income.

## 1.3 State/territory tax reform

CPA Australia acknowledges that the state/territory tax reform process under the GST Agreement has delivered significant benefits. However, the process has stalled with the failure of all jurisdictions to agree to abolition of stamp duties on business real property transfers notwithstanding the additional assistance promised by the Commonwealth. The reform process needs a 'kick-start' in order to secure an appropriate timetable for the abolition of the remaining duties listed in the Agreement.

Further reforms of the remaining inefficient state/territory taxes need to be addressed by the Commonwealth and the states through the COAG process. Such reforms could include reductions in the existing inefficient taxes on general insurance, removal of pay-roll tax anomalies, land tax reforms and restructuring of existing motor vehicle taxes.

CPA Australia has made submissions to the Victorian and WA Governments on these issues but believes that a broader approach through COAG with Commonwealth support would provide a better opportunity for further reforms to state/territory tax regimes.

### Recommendation

- CPA Australia would like to see further reforms of the remaining inefficient state/territory taxes addressed by the Commonwealth and states through the COAG process.

#### 1.4 Statutory privilege for clients of non-legal tax advisers

An ongoing problem for accountants in their dealings with clients on tax law issues is the absence of legal professional privilege (LPP) which applies under common law to dealings between lawyers and their clients. To create a level playing field in this area, CPA Australia believes LPP should be extended to non-legal tax advisers, such as accountants, by way of special legislation as has been implemented in jurisdictions such as New Zealand.

Given the increasing complexity of Australian taxation law and the fact that accountants continue to provide the great majority of taxation advice, it is anomalous that clients of legal advisers should be entitled to claim LPP in respect of tax advice while clients of non-legal tax advisers are not entitled to similar protection from disclosure.

The ATO has sought to remedy the above situation to some extent by providing an accountants' concession on an administrative basis which purportedly restricts access to professional accounting advisers' papers in some circumstances. However, the accountants' concession is only available for certain types of documents specified by the ATO and is also more limited in that it is based on a 'dominant' rather than a 'sole' purpose test as applies in the case of LPP. Since the ATO is not legally bound in respect to the accountants' concession, it still reserves the right to access accountants' papers in exceptional circumstances which is ultimately subject to determination by the ATO.

##### Recommendation

- CPA Australia recommends that the Government considers the introduction of statutory privilege for accountants similar to LPP as has been implemented in New Zealand.

#### 1.5 Volunteers and deductible gift recipients

Volunteering makes an important contribution to the health and welfare of communities and also provides much needed services at a lesser cost to the public purse.

##### Recommendations

In recognition of the contribution of volunteers to communities around Australia, CPA Australia recommends:

- The Government makes a tax exempt annual payment to volunteers.
- Alternatively, volunteers who make a contribution to deductible gift recipients be allowed a rebate or deduction for certain costs incurred (such as travel, uniforms etc.) in respect of these activities.

## 2.0 Superannuation reform

CPA Australia acknowledges and welcomes the broad thrust of the Government's plan to simplify and streamline existing superannuation arrangements as announced in the Budget and subsequently modified to some extent following consultations with relevant stakeholders. We believe, however, that some further improvements can and should be made to the new system both to ease the transition to the new regime and also to enhance it.

### 2.1 Extend deductibility of superannuation contributions

In recent times, employment arrangements have become more flexible with many people employed under casual or contracting arrangements. Those who consider themselves largely self-employed have found they may have lost their eligibility to claim a deduction for superannuation contributions after taking on relatively small consulting or contracting roles. There is often a 'double whammy' effect in that these contracting roles will only pay superannuation guarantee (SG) contributions and there is no provision for the contractor to make voluntary or salary sacrifice contributions. The result is individuals may end up with minimal superannuation coverage since they do not have any more than SG coverage from their employment and are not able to claim a deduction for their own contributions.

These individuals are at a distinct disadvantage compared to those who are full time employees or full time self-employed. As such, CPA Australia recommends the '10% rule' be abolished to provide greater incentive and flexibility to people who have to make their own superannuation provisions.

CPA Australia recognises such a move would also allow employees to claim a deduction for their personal superannuation contributions. However, with full deductibility being given to personal contributions, there is now essentially no difference between the treatment of employer, salary sacrifice and personal deductible (i.e. self employed) contributions and therefore no rationale as to why such deductibility is not permitted. The proposed \$50,000 annual limit on concessional contributions would control the concessions available and there would be no benefit in exceeding the limit as excessive contributions would be taxed at the top marginal tax rate.

Importantly, allowing deductibility for personal contributions would benefit those employees whose employers limit or do not provide for salary sacrifice contributions and are at a distinct disadvantage compared to employees who do have access to salary sacrifice

Abolishing the '10% rule' would create a level playing field whereby all superannuants would have the same access to concessional contributions and the same flexibility to decide whether their voluntary contributions should be made from before or after tax income. The limits on concessional and undeducted contributions would ensure everyone receives the same concessions. Such a move would be another important step in ensuring equity and simplifying the superannuation system.

#### Recommendation

- Abolish the '10% rule' for the deductibility of superannuation contributions to provide greater incentive and flexibility to people who have to make their own superannuation provisions.

### 2.2 Default scheme for voluntary personal contributions

Modelling conducted by the National Centre for Social and Economic Modelling (NATSEM) for CPA Australia, and contained in the report *Superannuation: The right balance?*<sup>1</sup> shows the 9% compulsory superannuation guarantee will only provide an adequate standard of living in retirement for an individual on average earnings when received over their whole working life. For those earning above average earnings or with broken work patterns, the SG alone will not be enough. It is recognised that a savings level of 12% to 15% is needed to maintain standards of living in retirement.

Voluntary contributions, above the compulsory 9% amount, are one way to fill the gap. However, the level of voluntary contributions has been falling since the late 1990s. While it is yet to be seen if the introduction of the co-contribution will arrest the decline, one way to encourage voluntary contributions would be to introduce a default scheme whereby voluntary contributions were automatically deducted from an employee's salary unless they chose to 'opt out' of the scheme. Such a scheme could commence at 1% of salary and increase to 3% over three years. Similar schemes operate very successfully overseas.

#### Recommendation

- Introduce a 3% voluntary superannuation contribution scheme.

<sup>1</sup> Superannuation: the right balance? NATSEM, CPA Australia, 2004



### 2.3 Superannuation guarantee threshold

The superannuation guarantee earnings threshold of \$450 per month was introduced when SG commenced at a level of 3% of salary. Since then the SG level has increased to 9% and the workforce has become increasingly casualised.

As a result more people are at risk of being excluded from the SG system and not having access to adequate retirement savings. For example, an individual who is working two or three casual jobs, each earning just under the \$450 threshold each month, could be missing out on SG contributions of \$800 to \$1200 each year.

#### Recommendation

- CPA Australia recommends the SG threshold of \$450 per month be abolished so as to boost retirement savings, particularly for people with broken or casual work patterns.

### 2.4 Superannuation simplification

Subsequent to the finalisation of *A Plan* to simplify and streamline superannuation in September 2006, CPA Australia believes there are still a number of areas of complexity that need to be addressed, including:

- Death benefits
- Commutation of existing complying pensions
- Concessional contribution limits
- Overseas benefits excluded from contribution limits.

#### Death benefits

It is proposed that the payment of death benefits to dependants after 30 June 2007 will be tax free, while the taxable component of death benefits paid to non-dependants will be taxed at 15%. CPA Australia believes this will provide arbitrage opportunities and create inequities within the system. For example, an individual knowing they are going to die will be able to take their superannuation benefit as a lump sum and pass it on to their adult children tax-free. On the other hand, where death is sudden and unforeseen, the benefit may still be paid to the adult children but it would be taxed at 15%. Additionally, re-contribution strategies are already being promoted in the market to withdraw the taxable component over time and re-contribute it as an undeducted contribution, effectively reducing the taxable component to nil.

#### Recommendations

- CPA Australia recommends all superannuation death benefits should be tax free after 30 June 2007 not just those to dependants.
- To further remove the incentive for these schemes and arbitrage, CPA Australia recommends that the current inconsistencies between the definitions of 'dependant' in the SIS Act and the Income Tax Assessment Act 1936 be removed by aligning the definition of child in the ITAA 1936 with that in the SIS Act.

## 2.5 Commutation of existing complying pensions

The proposed simplification of the pension rules from 1 July 2007 will result in complying income streams – lifetime, life expectancy and market linked – essentially being redundant (except for current recipients wishing to preserve their 100% or 50% asset test exemption). As one of the objectives of the proposed changes is to provide retirees with the flexibility to decide when and how they access their superannuation, CPA Australia recommends the pension and annuity standards be amended from 20 September 2007 to remove the commutation restrictions for existing complying income streams.

The commutation of commercially provided guaranteed income streams may have the potential to have a detrimental impact on members. However, there would be no such impact on recipients of market linked income streams (MLIS), and SMSF pensioners should be able to determine the impact themselves. Further, as MLIS are relatively new and they have been purchased in good faith to satisfy particular rules, individuals should be allowed to get out of these products, if they choose, now the rules have changed.

### Recommendation

- Commutation of existing complying income stream to be permitted from 20 September 2007.

## 2.6 Concessional contribution limits

While the new limits on deductible contributions will provide greater flexibility for younger contributors, and CPA Australia supports them, older contributors may be disadvantaged in the short term. Many people have significant financial commitments, such as family, education and mortgages, well into their late 40s and early 50s and as such have planned on making large superannuation contributions closer to retirement to catch up, as permitted by the current rules. This situation has been recognised and is reflected in the five year transitional period proposed. However, CPA Australia believes these arrangements are still too restrictive and unfairly penalise people who may have retirement savings plans in place based on the current rules. For someone aged 50 their options have been reduced from \$105,113 (plus indexing) a year for 15 years to only \$100,000 a year for five years. Their potential retirement savings have dropped considerably.

CPA Australia recommends that the transitional limit for individuals aged 50 and over be increased to \$100,000 for 10 years. This would permit more people, especially those in the over 50 group, who could have contributed the higher amount and had planned to, to fulfil their retirement savings plans.

### Recommendation

- The transitional period for the cap on concessional contributions for over 50s to be extended to 10 years.

## 2.7 Overseas benefits excluded from contribution limits

CPA Australia believes benefits transferred from overseas superannuation funds should be exempt from the contribution limits. Given these benefits are treated as if they have been accumulated in the Australian superannuation system, i.e. they are taxed accordingly, the individual should have the opportunity to add them to their Australian superannuation benefits. Applying the limits may actually make it difficult, if not impossible, for individuals to transfer their retirement savings into Australia as there will be situations where overseas funds will not permit partial transfers of benefits. As such, the transfer amount should be exempted from the limit on undeducted contributions and the amount elected to be treated as taxable contributions, i.e. the earnings should be exempted from the concessional contribution limit.

CPA Australia understands from previous discussions with Treasury officials that there may be concerns that such an exemption may provide the opportunity for individuals to funnel contributions through overseas superannuation funds and hence bypass the contribution limits. However, the risk of this is low, due to the difficulties involved with residency, termination of employment, taxation and payment rules, compared to the importance of allowing, and encouraging, expatriates to consolidate their retirement savings in Australia.

### Recommendation

- Transfers from overseas superannuation funds should be excluded from the contribution limits.

## 3.0 Skills shortage and workforce participation

The demand for accounting professionals continues to outstrip the availability of skilled professionals. Accounting has been included in the Migration Occupations in Demand List (MODL) which gives visa seekers with accounting skills an advantage in gaining selection for a visa under the General Skills Migration (GSM) Program. However, despite a significant number of visa approvals, there has been little impact on the skills shortage of accountants as many of those visaed applicants who are genuine in their desire to find employment in the accounting profession, do not have the requisite level of English proficiency to meet employer needs.

CPA Australia is very supportive of moves by the Government to increase the level of English competency required for GSM visas and for more emphasis to be placed on work experience in the GSM Points Test, however these initiatives alone will not resolve the issue of accounting shortages.

Universities consistently fill their allocation of HECS funded places for domestic students wanting to study accounting based degrees. In addition, many universities have complemented these with a growing number of full-fee paying places to the point where fee paying places outnumber HECS places. It is essential to ensure there is a balance between HECS funded places and fee paying places and that universities appropriate accurate resources to areas of highest demand.

As well as new entrants to the market, aspects of the skills shortage can be addressed by encouraging those who are leaving the employment market to stay longer and those temporarily out of the market to return. During 2005-06, CPA Australia undertook a project to identify the barriers to mature age accountants remaining in the workforce. The project identified that while there are accountants looking to stay active, major barriers to their successful employment are the preconceptions of employers and recruitment firms about older workers. CPA Australia will continue to develop strategies to assist older professionals. However, a national coordinated awareness and education strategy that includes all elements of the employment chain is needed to overcome prejudices.

### Recommendations

To alleviate the shortage of professional accountants, CPA Australia would like to see an integrated program of support which includes:

- Increased emphasis on English language skills and work experience when assessing skilled migration visa applications.
- Stronger requirements for universities to provide English language training for international students.
- Provision of funding to universities to incorporate work experience placements for accounting students.
- Additional support for skilled migrants to develop English language and work experience once they leave university.
- Encouragement for universities to allocate more HECS places to accounting-based disciplines.
- Increase in the overall number of domestic accounting HECS funded places.
- Coordinated national strategy to debunk negative perceptions about older employees.

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