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Introduction

As South Australia’s peak Chamber of Commerce and Industry, Business SA is South Australia’s leading business membership organisation. We represent thousands of businesses through direct membership and affiliated industry associations. These businesses come from all industry sectors, ranging in size from micro-business to multi-national companies. Business SA advocates on behalf of business to propose legislative, regulatory and policy reforms and programs for sustainable economic growth in South Australia.

Business SA’s submission to the State Tax Review Discussion Paper outlines our preliminary position on State tax reform and is part of a broader process involving the recently released Federal Tax White paper. As indicated at the recent business seminar on the State Tax Review, Business SA expects both the State and Federal tax review processes to deliver a tax system which provides the optimum level and structure of both State and Federal taxes. Businesses are agnostic as to whether or not they pay State or Federal taxes, but they are demanding a system which the State Government has advised needs to ‘support entrepreneurship, investment and job creation’.

Business SA views the State Tax Review primarily as a starting point and we will more holistically develop our position on key aspects of the tax system in parallel with the progress of both State and Federal tax reviews. Moreover, Business SA is consulting its membership throughout the tax reform process and is being guided by a tax expert member reference group.

The focus of our submission is primarily on the taxes which more broadly impact the decisions on businesses and which are most detrimental to the broader State economy.

As the voice of business in South Australia, we are genuinely encouraged by efforts from both the State and Federal Government to open the debate on tax reform. While the task of tax reform will always be a challenge for Governments, it is important that both levels of Government understand that competitive tension throughout the process will ultimately lead to optimum public policy outcomes. Stakeholder groups like Business SA must act in the best interests of members and whether or not we agree or disagree with either level of Government’s agenda, our approach will never be deliberately obstructionist. Likewise, Business SA expects both the State and Federal Governments to not only collaborate with business, but to also collaborate with one another for the best interests of business.

Tax reform is a once in a generation opportunity and considering South Australia’s current economic malaise and the challenges we face beyond auto-manufacturing, it is certainly not one we can afford to squander.

Should you require any further information or have any questions, please contact Rick Cairney, Director of Policy, Business SA on (08) 8300 0000 or rickc@business-sa.com.
Executive Summary

Business SA commends the State Government for opening the debate on State tax reform, particularly for being ahead of other jurisdictions including the Federal Government. However, it is important to recognise that meaningful tax reform must be undertaken as a collaborative process between State and Federal Governments. We support the State Government’s approach to firstly ‘get its own house in order’, but the best outcomes for business and the broader economy will only be achieved through an optimum mix of both State and Federal taxes.

While there have long been debates on the nature of existing taxes, particularly payroll tax and the GST, the tax reform process also needs to grasp the opportunity to re-imagine what might be possible. Notwithstanding the challenges of reinventing the tax system, a once in a generation opportunity to review both State and Federal taxes must be capitalised upon.

Whatever the ultimate outcomes of both State and Federal Tax reforms, South Australian businesses need a system which encourages investment and job creation. Furthermore, as South Australia enters a period of structural economic adjustment post auto-production, the tax system needs to appropriately incentivise the commercialisation of research and innovations, particularly to increase collaboration between the university sector and SMEs.

Reform of payroll tax will still be a primary focus of business in the tax reform process, but business is also interested in reforms which can improve the broader efficiency of the tax system and facilitate economic growth. Replacing stamp duty with land tax may improve the broader economy by enabling both businesses and residents to more easily move to their preferred location, but transitional measures will need to be appropriately set and considerations be made for how such changes might impact upon tenants, both commercial and residential.

The tax reform process should also capture compliance costs for business and where possible reduce or eliminate the burden on small business. In a recent survey of members relating to State based red tape, Business SA found taxation was the second largest impost of red-tape behind workplace, health and safety standards. For example, the present system of land tax aggregation imposes significant red-tape and we are pleased the Government is reviewing options for a more efficient system.

The Economic Case for Change

The South Australian economy continues to stagnate, with Gross State Product growing at just 1.3% during 2013/14. The latest State Final Demand figures for the six months to December 2014 also indicate declining economic growth for the financial year 2014/15. Beyond that, Gross State Product is forecast to grow at just 2.5% in 2015/16, before declining to 2.25% for both 2016/17 and 2017/18 as the South Australian economy adjusts to the loss of its automotive production sector.

Hopes of South Australia playing a significant role in the mining boom have been delayed by low mineral prices, particularly iron ore, while falling oil prices have depressed the short term outlook for the State’s unconventional gas prospects. On a brighter note, a recent run of average or above average grain crops have boosted the State’s agricultural prospects, as have higher beef prices. Furthermore, horticultural crops including almonds and citrus are showing particularly strong promise. The recent decline in the Australian dollar has also helped to support South Australia’s significant wine producing sector.

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1 ABS, Australian National Accounts 2013/14, 21 November 2014
2 South Australian Government, Mid-Year Budget Review, 2014
As at February 2015, South Australia’s unemployment rate stood at 6.9%, the highest of all States and Territories. Unfortunately this is combined with the 2nd lowest labour force participation rate amongst the States and Territories, which reflects both an ageing population and low confidence amongst job seekers. Youth unemployment at 23%, is 3% above the national average, and is reflected in apprenticeship commencements which have decreased from approximately 7,000 per quarter as at July 2012 to approximately 3,000 per quarter as at September 2014.3.

The State Government’s analysis shows a falling age dependency ratio from 1.9 (working age people to dependents) in 2014 to 1.5 by 2031, a decline of over 26% in just 17 years. With significantly less people working to support those underage or past retirement age, it becomes even more critical that the tax system incentivises investment to create economic growth and job creation to ensure South Australia is able to meet the challenges of an ageing population.

Approach to Tax Reform

The discussion paper is a solid starting point for consultation and conversations about State tax reform, but the Government should also consider what the State tax system could look like if it started with a blank slate. What would be the optimum design of State taxes if the colony of South Australia was being established in 2015, not 1836? How would it encourage businesses to invest and employ people? What revenues would be required and what would be the justification for taxing certain sectors to raise necessary revenues? What would be the optimum tax burden on business and individuals in order to maximise economic growth and employment levels while enabling a fair distribution of economic prosperity?

Subsequently such proposals would need to allow for transitional measures where the short term impact on specific taxpayer classes are severe. However, the opportunity to undergo root and branch reform of South Australia’s tax system should not waste the chance to rethink the entire structure of State taxes.

Business SA supports the State Government’s comments that:

- ‘Business must pay its fair share of State taxes, but the taxes paid by the business sector should not stand in the way of those who are actively investing in creating job opportunities.’
- ‘Our tax system should support entrepreneurship, investment and job creation, increasing the overall prosperity of the State.’
- ‘It is important, however, that all sectors of the community pay their fair share of taxes. Therefore future reforms are not intended to simply exempt certain sectors from State Taxes. Instead the Government intends that any reforms to our tax system should make South Australia an attractive place to do business and ensure the State remains an affordable place to live for all South Australians.’

3 NCVER, September Quarter 2014, P18
There is still a large degree of uncertainty over what the future holds for companies in South Australia’s automotive supply chain once Ford’s Victorian factories shut in 2016 and Holden ceases manufacturing in 2017 with Toyota in close succession. While there is some Government assistance to help component suppliers transition to new industries, diversification opportunities in an otherwise weak economy are quite limited and many companies are internationally domiciled with no strategic drivers to diversify their businesses solely to remain in South Australia. Furthermore, diversifying traditional automotive component manufacturers is a difficult and lengthy process. As a result there is likely to be significant unemployment issues in the short to medium term once excess workers are laid off with limited opportunities available in the broader economy, particularly if South Australia’s naval shipbuilding industry does not materially benefit from the future submarine or frigates project.

The State Government should be considering how the tax system can better encourage commercialisation of innovative research to ensure the long term economic outcomes South Australia needs to diversify its economy are realised. Whether or not this is ultimately facilitated through changes at either a State or Federal level, South Australia should take a leadership position in advocating for the type of tax arrangements which will help fill the void left by auto-manufacturing.

**Revenue Neutrality**

Business SA has long opposed the level of business taxation in South Australia and we have relentlessly lobbied for a more efficient public sector to enable the Government to be in a position to cut business taxes. We commend the State Government for adopting several recommendations from our *2014 Charter for a more Prosperous South Australia* (the Charter), most notably relating to WorkCover reform which will save employers $180 million per annum, and we continue to advocate and lobby for the remaining recommendations to be adopted.

Notwithstanding our ongoing advocacy efforts relating to a broad range of issues impacting business, particularly small business, we accept the premise upon which the State Tax Review takes place; that being on the basis of revenue neutrality. While we do not necessarily accept the level of any individual State based tax, we recognise the need for wholesale tax reform and for the Government to be able to maintain its revenue base; at least in the short term.

Accordingly, we will continue to advocate for more efficient public sector spending, but not necessarily on the basis of enabling specific tax reform measures. However, we acknowledge that the State Government will take a conservative approach to revenue forecasts from tax reforms and we expect any windfall gains from tax reform to be returned through reduced business taxes. If organisations like Business SA are expected to collaborate in good faith to achieve wholesale tax reform, it follows that we require a commitment that the total tax impost on our members will not increase following any agreed changes.

**South Australia’s Tax Impost on Business**

Business SA does not consider the State Tax Review to be the forum for debating the various non-Government reports which benchmark State taxes. Notwithstanding, it would be remiss of us not to mention the 2014/15 State Tax Review just released by Pitcher Partners which ranks South Australia as having the least competitive State tax regime for start-ups who choose to rent. Although we recognise that the same report ranks South Australia as being the most competitive State for a business wishing to purchase property, the vast majority of small businesses are not in a position to buy property, nor is it necessarily fundamental to the success or otherwise of their businesses. Furthermore, low demand for commercial property in South Australia actually reflects the broader level of demand in the State economy and is not necessarily reflective of a tax structure which
encourages business, particularly small business. It is simply fortuitous that weak economic demand often translates to low property prices and we should not forget that property markets are invariably cyclical.

The Commonwealth Grants Commission’s assessment of South Australia’s relative tax effort being 10% above the average of all the States and Territories is a reminder that our economy, including individuals and businesses, is being hamstrung by an inefficient level of public spending. This has only been exacerbated by consecutive budget deficits, a trend which was already visible before any Federal Government spending reductions in last year’s budget.

### Payroll Tax

Business SA has over 5,000 member businesses which we consult with on an ongoing basis to ensure we effectively advocate their needs. The State Government may not agree that payroll tax is a ‘tax on jobs’, but we are guided by what our member businesses advise us and the way in which they behave in response to specific taxes such as payroll tax. Payroll tax is limiting the expansion of businesses, particularly those below but approaching the tax free threshold, and does actually prevent job creation by small business. Whether or not this can be proven by empirical data, it still remains that the overwhelming anecdotal evidence shows that businesses’ hiring behaviour is being distorted by the presence of payroll tax. Payroll tax is also very difficult for small businesses to rationalise for it does not seem logical that they are penalised for employing people beyond a specified threshold.

Business SA surveys members on various tax reform options and can disclose the following:

- In our September Quarter 2013 Survey of Business Expectations, when members were asked which State taxes or levies were most limiting to the expansion of their business and, if given the choice which would they reduce or abolish; a little under half (approximately 49%) of businesses surveyed nominated payroll tax. Other limiting State taxes or levies were WorkCover (24.1%), Stamp Duty (19%) and Land Tax (8%).

- In our pre-2014 election survey, members ranked ‘progressively raising the payroll tax threshold’ as the most important tax reform.

Business SA acknowledges the following excerpt from the discussion paper:

‘An important factor when considering the fairness of a tax is who actually bears the ultimate cost. This can be different to the party that is legally required to pay the tax. For example employers are required to pay payroll tax, but as noted in various tax literature, the long-run incidence of payroll tax most likely falls on consumers or employees through increased prices or reduced wages.’

If the long-run incidence of payroll tax is absorbed by employees through reduced wages and by consumers through increased prices, there is logic to suggest that the long-run effect of replacing payroll tax with an increased GST should be to balance employee welfare through higher wages offsetting increased consumer prices. Concurrently, employers will be incentivised to create more jobs which will increase demand in the labour market and further increase employee welfare. Such an option should be modelled as part of the State Government’s existing work through Deloitte Access Economics and be presented in any subsequent draft report for further consultation and feedback.

In the lead up to the 2010 election, former Premier Mike Rann announced a four year relief plan promising to abolish payroll tax for apprentices and trainees, but this tax exemption was subsequently abolished in the 2012/13 Budget. The resultant savings were supposedly redirected to better target support for training in areas of critical skills under the new Skills for All program. However, under Skills
for All virtually all non-trade qualifications have been capped and subsidies for the few funded qualifications which directly link to employment outcomes have been significantly reduced. Subsequently, the Government has acknowledged that Skills for All has not delivered the outcomes that are needed and subsequently has scrapped the program.

In a survey of its members, Business SA found that if the payroll tax exemption for apprentices and trainees had remained in place, three quarters of respondents would have employed more apprentices, and almost two thirds of respondents would have employed more trainees. This accords with the actual reported level of apprenticeship commencements which have decreased from approximately 7,000 per quarter as at July 2012 to approximately 3,000 per quarter as at September 2014.

International payroll tax equivalents are typically for specific social security requirements and are not necessarily entirely paid for by employers. Furthermore, not all comparable countries even levy payroll tax, including New Zealand. Moreover payroll tax is still considered a relatively inefficient tax, particularly when compared with the GST and business representative groups expect the State Government will model all options to abolish or at least substantially reduce payroll tax. Whether or not such tax reform requires State/Federal collaboration is irrelevant for businesses that just want to operate in an environment which does not penalise them for employing people. This is particularly so in a State which has the highest unemployment rate in the nation, a high youth unemployment rate and the second lowest labour force participation rate.

GST

The GST provides the largest single source of South Australian tax revenue and cannot be ignored in any genuine attempt at State tax reform. The GST is also a highly efficient tax, being more efficient than payroll tax, and would be even more efficient if its base was broadened to include all existing exempt goods and services. As a start, the GST should apply to imported goods above at least $100 in value, abolishing most of the existing exemption where GST is only payable beyond a $1,000 threshold. At the $100 threshold, the Federal Government has determined enough GST revenue would be collected to offset the additional costs of administration.

Business SA agrees that Federal/State tax reform does not necessarily have to leap to a debate on the GST, but by the same token, no comprehensive tax reform can ignore the size and scope of the GST if we are to have a more efficient tax system.

The fact that South Australia is limited to amending the GST of its own accord should not be a barrier to pursuing a collaborative approach with the Federal Government and other States. Business SA has been pleased to see the State Government show leadership on tax reform ahead of the Federal Government and despite inaction by other States, and expects that approach to extend to facilitating constructive debate on the GST.

Business SA acknowledges the State Government’s approach on the GST which is summarised below:

‘If options to reform the GST are to be considered, fairness must be a key objective’.

4 NCVER, September Quarter 2014, P18
5 ABS, Labour Force, Australia, March 2015
6 Low Value Parcel Processing Threshold Taskforce, July 2012, P9
However, we remind the Government that it also states that the key principles for State tax reform include:

- Efficiency;
- Equity;
- Simplicity; and
- Sustainability.

The evidence suggests the GST is very efficient and is also relatively stable when compared with taxes such as stamp duty. Furthermore, if the GST is broadened, its simplicity will improve and it is equitable in the sense that no one, no matter how good their accountant, can avoid paying the GST on a meat pie at the Adelaide Oval. While Business SA accepts the GST may not be a ‘progressive’ tax, the reality is that it ticks many more boxes than other State and Federal taxes being considered for reform and it would be a lost opportunity not to at least consider how reform of the GST could enhance South Australia’s tax system.

As Business SA has previously indicated in discussions with the State Government, we support the existing structure of Horizontal Fiscal Equalisation (HFE) and do not see potential reform of this system as a barrier for beneficiary States like South Australia to rigorously pursue debate on the GST base and rate. It remains our view that in the long run, all States benefit from HFE and any short term lobbying by States such as Western Australia will soon settle in line with commodity price cycles.

The State Government may also be able to achieve reforms on highly inefficient insurance taxes, an impost on both businesses and households, through restructuring the GST.

**Stamp Duty & Land Tax**

While Business SA acknowledges there may be long term benefits for businesses and residents from not having to pay stamp duty, any transition to a system of broad based land tax will need to be carefully managed to avoid double taxation, particularly for elderly people who may be asset rich and cash poor due to the nature of long term property cycles, particularly in the more recently gentrified suburbs of Adelaide.

The Government’s suggestion of a form of credit bank for previously paid stamp duty seems logical, but it may not necessarily provide for all circumstances of businesses or residents; which should be uncovered through the consultation process.

While it will be advantageous for some businesses to be able to shift premises without being restricted by considerations of stamp duty, imposing a broad based land tax may also shift more of that impost onto commercial tenants, either directly or through increased rents. It will be important that the State Government comprehensively models the impact on businesses which both rent and own their premises before organisations such as Business SA are able to adequately comment on the holistic outcomes for member businesses.

South Australia’s land tax regime is well understood to be the least competitive in Australia and the business sector has long argued for land tax relief. If a business owns a $1 million site in South Australia and pays $9,446 in land tax versus $1,750 for a comparable site in Western Australia, this puts our members at a significant disadvantage. Even the Commonwealth Grants Commission reports South Australia as imposing a land tax burden 36% higher than the average of other States and Territories.
Land tax reform should also address the existing inefficiencies in how land tax is levied upon entities and potentially move towards a simpler system based on Eastern States practice. However, we recognise the inherent difficulties associated with identifying properties in joint ownership and the State Government needs to be careful to ensure it does not replace one system with another one which can just as easily be circumvented via accounting loopholes.

The State Tax Review needs to clearly differentiate between stamp duty on real and non-real property transfers. Anecdotal evidence suggests South Australia’s lack of action in removing stamp duty on non-real property transfers is acting to discourage interstate investors in local companies, particularly when coming from States such as Victoria which have already abolished such taxes.

In Business SA’s 2014 Charter, we recommend the State Government abolish stamp duty on business transfers and non-quotable marketable securities as agreed in the Inter-Governmental Agreement on Federal Financial Relations. Such reforms should not necessarily hinge on outcomes related to broader reform of stamp duty.

**Royalties**

Business SA supports South Australia’s relatively competitive royalty system, particularly at a time of depressed commodity prices. It will be important that any amendments to the existing system not act to discourage exploration efforts nor increase the threshold level for existing projects to commence. South Australia has substantial long term mining and unconventional gas prospects and while some of these prospects may not necessarily be viable in the short to medium term, the tax system still needs to encourage companies to take a long term view of South Australia and continue to invest at the pre-feasibility stage.

**Gambling Taxes**

Notwithstanding there are various social policy considerations for the State Government in relation to gambling taxes, any changes which impact upon the existing viability of not-for-profit community based clubs need to be appropriately accommodated for. Furthermore, while Business SA accepts the State Government is keen to reform gambling taxes on the basis of increased efficiency, then likewise the State Government must consider the increased efficiency of its tax base which would emanate from GST reform.