



TOTAL ENVIRONMENT CENTRE INC

# SUBMISSION TO THE AUSTRALIA'S FUTURE TAX SYSTEM REVIEW

May 1<sup>st</sup>, 2009

## Introduction

Australia's Future Tax System (the AFTS) represents an historic opportunity to bring the taxation system, a major lever in our economy, into greater alignment with environmental, social and economic imperatives to drive action on climate change and wider issues for a sustainable society.

The AFTS review is expected to set the stage for the tax system for the next 20 years or even longer, and is likely to identify key areas for further investigation over the next several years as well as recommend specific reforms for more immediate implementation. In that 20-year plus timeframe, covering the next generation and beyond, sustainability will become a pillar of government policy. Sustainability also will become an integral part of a tax system that is fair and effective, rather than an environmental and/or social add-on.

The AFTS consultation paper rightly says:

*'Australia faces significant environmental challenges in the 21st century, ranging from global issues, such as climate change, to local issues, such as water scarcity, land degradation and species loss. Economic development must be undertaken in an environmentally sustainable way, while also recognising that the environment itself has value. Taxes may provide one means of improving environmental amenity. The tax-transfer system can also detract from environmental outcomes through the incentives it creates. Such incentives need to be carefully evaluated against other policy objectives.'*

As Australia debates the Carbon Pollution Reduction Scheme (CPRS) in 2009 it becomes clearer by the day that starting the transition to a low-carbon, more sustainable economy can't just be left to a single market-based mechanism (i.e. a 'cap and trade' emissions trading scheme); much more is required.

We need strong market interventions through direct regulation, additional or complementary measures such as renewable energy and energy efficiency targets, and of course – reform of the taxation system. The Total Environment Centre (TEC) believes Australia, via the AFTS, must seize this unprecedented opportunity to harness the tax system to help drive the nation towards a more sustainable future – environmentally, socially and economically.

So what is the role of the tax system in delivering the greener, more sustainable economy we desperately need on economic and environmental grounds? TEC has taken a strong interest in tax because we know government uses it as a lever to change

business and individual taxpayer behaviour, as well as its principal purpose to raise revenue to pay for running government administration, services and programs.

Our submission does not ask the AFTS to recommend discreet so-called 'environmental taxes'. Rather, we argue in alignment with the AFTS' own terms of reference and its consultation paper that reform of the taxation system is a prerequisite for a mainstream transitioning to a low-carbon, sustainable path in the 21<sup>st</sup> century. Australia's tax system needs to be substantially reshaped to raise revenue for government services and programs, in equitable and transparent ways, while also assisting to propel delivery of better environmental and societal outcomes.

## **Our Process**

This submission has been developed by the TEC and its corporate sustainability arm, the Green Capital program, as part of our two-year S3i initiative to shift Australia from unsustainable 'short-termism' in business and political decision-making to longer-term sustainability based on the right 'incentives, innovation and investment'. Our process has included:

- An extensive review of early submissions made to the AFTS in 2008 and the AFTS consultation paper released prior to last Christmas
- Preliminary development of TEC priority issues and possible policy interventions
- Engagement with the AFTS secretariat
- Roundtable-style workshops in Sydney and Melbourne early in March 2009 to further develop understanding of the key issues, to refine TEC recommendations, and to generate further proposals for action
- Two major forum-style events attended by a total of nearly 300 mainly business and NGO delegates later in March 2009 – one in Sydney and the other in Melbourne – around the theme of 'Funding the Future: A green tax revolution?' (the AFTS secretariat was in the audience of both events and provided a speaker in Melbourne)
- Follow-up to synthesise all of the above to produce this submission.

## **Principles**

At a higher level than specific taxation measures that may be considered by the AFTS, we believe there are principles that should be used in framing and also evaluating 'sustainable' and 'green' tax reform proposals. Our focus is predominantly on environmental sustainability.

### **Principle 1 – The current tax system can and does harm the environment**

The current tax system does cause harm to the environment, including through perverse incentives that conflict with sustainability and climate change imperatives such as carbon pollution reduction and resource efficiency.

### **Principle 2 – The future tax system can and should help the environment**

The tax system is a legitimate tool for delivering better environmental outcomes as part of a successful and sustainable economy and is capable of exerting significant influence on business and individual consumers' behaviour.

### **Principle 3 – Tax reform is not a ‘silver bullet solution’ for sustainability**

Tax measures on their own are not necessarily the best way to drive change in behaviour and tax reform is likely to be most effective when integrated with other policy initiatives and economic levers.

### **Principle 4 – Sustainability advocates need a seat at the table to propose sound reforms**

The debate about the future of the tax system is not just one for existing beneficiaries and policy specialists, but must now centrally involve environmental stakeholders. This imposes a responsibility on proponents for change to articulate how new measures will operate fairly and effectively, and pay their way (i.e. through new/replacement revenue streams, greater productivity, reduced demands on the budget etc.)

### **The tax system at the crossroads**

The global recession now also gripping Australia is a mixed blessing for the environment movement. On one hand we’re being told we can’t afford to introduce emissions trading and other environmental measures because it will kill investment and jobs. On the other hand the emperor of the capitalist system has rarely looked more bereft of clothes. Governments are intervening in the financial markets massively, so why not do the same for the environment?

In fact, we’ve seen the US, the EU, Korea, China and other governments around the world making so-called ‘green stimulus’ a significant feature of their economic bail-out packages, and Australia has echoed the trend in areas like the \$6 billion ‘New Car Plan for a Greener Future’ and the \$4 billion ‘green home retrofit’ initiative.

‘Green skills’, ‘green jobs’ and a ‘green gold rush’ are now concepts being expounded by governments and the trade union movement, not just a few environmentalists. So what is the role of the tax system in delivering the greener, more sustainable economy we desperately need on economic and environmental grounds?

There are big issues and big dollars at stake:

- Australia is spending \$11 billion plus in a desperate attempt to save the environment and the economy of the nation’s food bowl, the Murray Darling Basin, yet we don’t realistically tax or ‘price’ the extraction of our precious water resource. As a consequence water was squandered.
- We have the Rudd Government’s \$6 billion new car plan for a greener future aimed at saving car manufacturing in Australia, but there’s no guarantee Australians will become overnight fans of locally-manufactured more fuel efficient vehicles without some other interventions, including tax reform.
- Currently Fringe Benefits Tax encourages company car beneficiaries to drive more rather than opt for green vehicles; the Luxury Car Tax focuses on sale price rather than pollution; and other provisions discourage companies from moving employees out of cars altogether and on to public transport.

- On the roads there's a question of whether traditional revenue-raising through fuel excises will continue to be effective to raise funds for building and maintaining roads. Fuel-efficient and electric vehicles will pay a lot less fuel excise, but they'll still want to use roads and will cause congestion. (A 2005 report for the Business Council of Australia estimated road congestion costs by 2015 at \$30 billion a year for Australia. In 2007 the federal Bureau of Transport and Regional Economics put the avoidable costs of congestion on Australian roads at \$9.4 billion in 2005 rising to over \$20 billion by 2020. The 2020 figure includes private time costs of \$7.4 billion, business time costs of \$9 billion, extra vehicle operating costs of \$2.4 billion and extra air pollution costs of \$1.5 billion.)

There are persuasive reasons to act.

## Timing

The closing time for written submissions to AFTS, May 1, 2009, places particular demands on our submission given that it deals primarily with matters relating to the environment, sustainability, climate change and the planned advent of the Carbon Pollution Reduction Scheme

Because the CPRS legislation will go to the Parliament after this submission is finalised, and given it faces an uncertain political future in the Senate, the TEC and Green Capital have framed a number of key recommendations with three main alternatives in mind:

- The CPRS starts in 2010 as proposed by the Australian Government
- The CPRS starts at some near-term later date e.g. in 2011 or 2012 at the latest
- The CPRS is postponed indefinitely, or at least until beyond 2012

Depending on if/when the CPRS starts, and exactly how it is framed, the taxation system may be legitimately called upon to play different roles in supporting and facilitating Australia's transition to a low carbon economy at the speed and scale required to avert or at least reduce the risk of dangerous climate change (i.e. at a minimum avoiding greater than 2 degrees Celsius rise in average global temperatures as a result of human-induced greenhouse gas pollution).

Ultimately this is not a matter of a few 'green measures' in a tax system that remains relatively unchanged. All tax measures, and all economic activity for that matter, will impact on the environment and climate action in some way. Economy, society and the environment are inter-woven, and sustainability is relevant to all. Emerging climate change policy is the biggest driver for real change in the outcomes for our society, our economies and the natural environment.

In their 2008 joint submission to the AFTS, top four accounting firm KPMG and the Institute of Chartered Accountants recommend:

*'An overarching review of the tax-transfer systems should be undertaken for consistency with the Government's climate change objectives. The tax-transfer systems need to be reviewed and, where appropriate, modified so they are consistent with the Government's climate change reform agenda. The tax-transfer systems should encourage behavioural responses to embrace reform sooner rather than later.'*

The TEC agrees whole-heartedly with the need for such an ‘overarching review’ which can advise the government on a course of action whatever happens with specific measures such as the CPRS, the new 20% by 2020 Renewable Energy Target (RET), a national energy efficiency strategy, a new national waste policy, the 10-year review of the Environment Protection and Biodiversity Conservation Act, and other major areas.

In this light, our submission makes the following two high-level recommendations:

**Recommendation 1:** Establish a follow-on ‘review’ or ‘task force’ to ensure that the tax-transfer system is consistent with the evolving objectives and direction of the government’s climate change action agenda, taking into account the likelihood that policy will continue to develop for a number of years after the AFTS makes its report.

**Recommendation 2:** Treasury and the Australian Taxation Office need to be effectively integrated into a well-coordinated, whole-of-government strategic effort with the flexibility to vary the mix of economic and market-based levers, including tax measures, based on:

- a) The overarching need to maximise timely and cost-effective emission reductions, *and*
- b) The variable importance that taxation may play as a lever depending on whether or not an effective emissions trading regime is implemented. (For example, in the event that the CPRS is delayed or does not proceed at all, and therefore there is no large pool of funds available to the government from auctioning emission permits, it may be appropriate to re-look at a carbon tax option and also to consider a range of tax incentives to drive energy efficiency, research and development and other activities.)

These recommendations are relevant to the broad framing of the AFTS review, and also to the AFTS consultation paper questions:

**Q3.4:** Assuming no increase in the rate or base of the GST, what principles should guide the future development of other consumption taxes in Australia, and is there a need to change the role and structure of such taxes?

**Q3.5:** Could greater application of user charges, rather than general taxes, in the funding of government services or infrastructure bring social, environmental or economic benefits?

**Q13.1:** Bearing in mind that tax is one of several possible instruments that can address environmental externalities, what opportunities exist to use specific environmental taxes to address Australia’s environmental challenges?

**Q13.3:** Given the environmental challenges confronting Australian society, are there opportunities to shape tax-transfer policies which do not currently affect the environment in ways which could deliver better environmental outcomes?

### **Specific Focus Areas for Tax Reform**

So what are the tax reforms we need to ensure a cleaner, healthier and wealthier future, while also having an eye to the immediate demand for stimulus to reinvigorate the Australian economy in the face of a global recession?

Based on the principles above and initial assessment by TEC and Green Capital, we have focused on:

1. **ROAD-USER CHARGING:** A longer-term shift to full-cost recovery road-user charging for cars and trucks, moving from the current fuel excise system to a user-pays, per-kilometre charge for road users enabled by satellite-tracking technology. This is consistent with emerging trends in North America and Europe, where fuel excise is starting to fail as the mechanism for funding roads as vehicles become more fuel efficient and in the future as we move to hybrid electric and fully electric vehicles.

**Recommendation 3:** Design a three-year COAG planning process with involvement of the National Transport Commission aimed at developing a per-kilometre charging regime for all vehicles on Australia's roads, coupled with measures to provide incentives for using public transport, car pooling or sharing and using greener vehicles; and also equity measures e.g. for people in rural, regional or urban areas not serviced by adequate public transport. The potential to raise additional monies to support public transport infrastructure improvements and expansion also should be considered as part of this reform.

This recommendation is relevant to the AFTS consultation paper questions:

**Q9.2:** Given the widely held view in submissions that the current state tax arrangements need to be reformed, what changes should be made to state and local government own source revenue instruments? What scope is there for greater use of user charging to bring social, environmental or economic benefits?

**Q12.1:** How can motor vehicle-related taxes and road funding arrangements be designed to improve the efficiency of transport of people and goods in Australia?

**Q12.2:** What should be the role, if any, of fuel taxes? What does this mean for how fuels and their uses are taxed and the rates of tax applied?

**Q12.3:** Do the existing tax arrangements lead people to make economically inefficient transport choices, and if so, how might they be improved?

2. **FBT & LUXURY CAR TAX** - Transforming Fringe Benefits Tax (FBT) provisions for company cars that perversely promote increased vehicle use, and creating FBT-related incentives for companies to assist employees to move from private vehicles for commuting to public transport, walking and cycling and/or flexible working arrangements such as tele-commuting. These measures should be aligned with greater investment in public transport and the government's \$6 billion car plan and its support for greener vehicles, and could be phased in over several years. Effectively, the tax system should be used as one of a number of mechanisms to foster demand for a) public and alternative transport options, and b) hybrid and more fuel-efficient vehicles, and to provide a disincentive for purchase of new larger and less fuel-efficient vehicles. The Luxury Car Tax should be extended to place an additional impost on fuel-inefficient luxury vehicles and to provide a concession for more fuel efficient ones.

GM Holden (in a submission to the AFTS) says: 'The statutory formula method for calculating FBT is based on the number of kilometers traveled and the statutory fractions are higher for lower kilometres (0.26 for under 15,000kms p.a.) and lower for higher

kilometres (0.07 for over 40,000kms). This method of assessing the taxable value of car benefits has been claimed to encourage unnecessary vehicle use. GM Holden's own experience, together with broader anecdotal evidence, suggests employees may drive extra distances to avail themselves of lower thresholds under the statutory formula method of assessing car fringe benefits. Not only is this inefficient, it clearly runs counter to national efforts to reduce carbon emissions.'

**Recommendation 4:** Make changes from the 2010 Federal Budget at the latest that can harness the FBT, the Luxury Car tax and potentially other measures to assist in fostering consumer and corporate fleet demand for greener vehicles, thus supporting the objectives of the Green Car Plan and overall restructuring of the Australian car industry. In addition, measures to promote use of public transport and to discourage private car/solo private car travel in favour of alternatives such as cycling, walking etc.

This recommendation is relevant to the below AFTS consultation paper questions:

**Q11.1:** Is it appropriate to use taxes on specific goods or services to influence individual consumption choices, and if so, what principles can be applied in designing the structure and rates of such taxes?

**Q11.6:** Should the tax system have a role in influencing the relative prices of different types of cars, including luxury cars and higher polluting cars, and if so, on what basis? What does this mean for taxes on the purchase price of motor vehicles?

**Q13.2:** Noting that many submissions raise concerns over unintended environmental consequences of taxes and transfers, such as the fringe benefits tax concession for cars, are there features of the tax-transfer system which encourage poor environmental outcomes and how might such outcomes be addressed?

- 3. ACCELERATED DEPRECIATION** - Accelerated 'green depreciation' for investment in energy-efficiency and other environmentally beneficial retrofits for buildings and also industrial facilities and equipment (including heavy manufacturing and mining). A particular focus on the waste management and recycling sector has recently been advocated as waste processing and recycling infrastructure is a key industry area where accelerated depreciation could drive investment and jobs; and prevent resources being wasted by going to landfill. In the case of building retrofits conditions should apply such as applying only to those with an inadequate commercial rate of return (i.e. greater than 3 years). In the case of other activity there could be 'sunset clauses' and employment guarantees.

**Recommendation 5:** Establish a national process for evaluating opportunities to apply accelerated depreciation in strategic areas such as the recycling sector (see below for more detail in 'Waste Recycling Sector Case Study'), and industrial restructuring, to drive jobs through energy and resource efficiency, and cleaner production.

- 4. NATURAL RESOURCE PRICING** - Rethinking the pricing of the royalties and rentals we put on our nation's precious natural resources, with a core objective to encourage sustainable use of renewable resources and reduce unsustainable use of non-renewable resources. While the principle of including externalities in pricing is becoming increasingly accepted – can the market operate sufficiently well to take account of scarcity? In theory higher prices can lead to access for previously uneconomic resources. However, in the transition we would see serious equity impacts; and some of the alternatives can have very high environmental impacts, for example from exploitation of oil sands or coal liquefaction.

We agree with the Australian Conservation Foundation (ACF) in its 2008 submission to the AFTS: 'The pricing of natural resources continues to be misaligned with actual market values for such resources. Despite some reforms, pricing of many natural resources is not clearly in line with national competition principles and the need to sustain renewable resources and conserve non-renewable resources. Comprehensive reviews of pricing of water, timber, mineral resources, fish, and oil & gas should be undertaken to ensure that rights to exploit such resources are priced at a minimum consistent with market prices on an ongoing basis, and in addition that long-term sustainability of renewable resources and steady reductions in the use of non-renewable resources are achieved.'

**Recommendation 6:** Establish a Natural Resources Pricing Authority to make public inquiries and advise governments on true-cost and true-value pricing for Australia's non-renewable and renewable resources including proper consideration of externalities and 'rarity value' in a resource-constrained world.

This recommendation is relevant to the AFTS consultation paper questions:

**Q14.1:** When considering the appropriate return to the Australian community for the use of its non-renewable resources, what relative weight should be given to the determinants of that return?

**Q14.2:** What is the most appropriate method of charging for Australia's non-renewable resources, given they are immobile but that Australia needs to compete globally for mining investment?

**Q14.3:** What is the role of the tax system in ensuring that renewable resources are used both sustainably and efficiently?

5. **GREEN JOBS AND SKILLS** - Specific measures to further encourage investment in R&D for green technology and services, their accelerated deployment and 'green skills training' including re-training in key areas such as building trades (i.e. construction, electrical and plumbing). The CSIRO report, 'Growing the Green Collar Economy' found that under a resource efficiency scenario (use of gas and renewables, energy efficiency, public transport, changed eating habits, etc) there would be employment growth of several hundred thousand jobs in the next 10 years, and more in 20 years, but there must be readily available skills, education and training.

**Recommendation 7:** Immediately review tax treatment to ensure that employers using downtime in the current recession to train employees in 'green skill' areas receive positive support via the tax system.

### **The Waste Recycling Sector Case Study– An opportunity to create jobs and drive investment through tax assistance and benefits**

The National Recycling Initiative (NRI) launched by the Boomerang Alliance (BA, a consortium of peak environment groups) and the Australian Council of Recyclers (ACOR) demonstrates how use of the tax system can achieve both major environmental and economic gains.



It's important to realise that the recycling sector (when reprocessing activity is included) is worth almost \$10 billion and 10,000 jobs to the economy each year. Increased rates of recovery of waste, diverting it from landfill and reprocessing into new commodities and products, can add approx. \$750 of value to each tonne of waste.

The NRI seeks to increase the pace of investment in recycling and reprocessing infrastructure through targeted federal and state assistance. A 50% accelerated depreciation allowance and allocation of state waste levy funds is being sought. Discussions with the recycling industry indicate some \$2 billion of new investment would be likely, creating about 6,000 jobs and abating over 1.5 million tonnes of greenhouse gases.

Calculations by BA and ACOR show that this will lead to around \$1.8 billion in new recycling and resource recovery activity; and as much as \$6.8 billion in associated economic activity. Conservatively this will generate over time some \$550 million in additional federal, state and local government revenue from the direct activities of recyclers plus another \$2.1 billion from downstream activity.

This would more than counter the 'costs' of using government tax arrangements (in accordance with the principles outlined above in this TEC submission to the AFTS). (Full report available on request).

**CONTACT:**

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