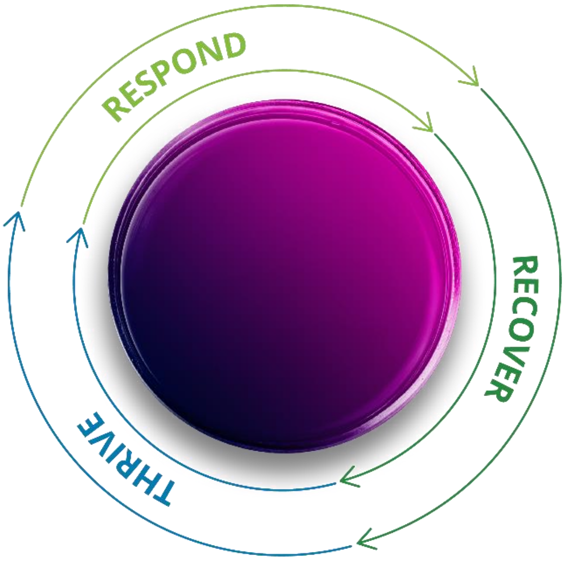
10 June 2020

Australia 2020/18



Tax Insights

Respond moving to Recover: Australia's initial tax policy responses to COVID-19

Snapshot

During the initial stages of the COVID-19 pandemic, Australia heeded the dire warnings of its scientists and medical professionals and approached the twin health and economic risks with the attitude "plan for the worst, hope for the best".

As early as January 2020, the Australian Government listed the coronavirus as a disease with pandemic potential under the Biosecurity Act and stood up our Incident Response Centre in Canberra. The expert medical panel was convened and met from 31st of January. On the 1st of February, the first of our border closures came into place. Since that time, we have seen unprecedent changes in our daily lives involving decisions across all levels of government, in respect of nearly every government department, to a degree of urgency and scope arguably greater than wartime. The changes have quickly permeated out to all businesses, all aspects of our schools and community and into households.

A first round of $17.6 billion stimulus measures was announced by the Federal Government on 12 March 2020 and further $66.1 billion economic support measures were announced on 22 March 2020. On 30 March 2020, the Federal Government announced further support in respect of a JobKeeper payment worth an estimated $130 billion (later recalibrated to $70 billion). In addition, further support was provided by way of Federal Government loan guarantees, $15 billion of support for smaller lenders and Reserve Bank measures.

Targeted measures were proposed for certain sectors (e.g., aviation, private hospitals). This is likely to continue: on 4 June 2020, the Federal Government announced a $680 million Homebuilder program to support jobs in the residential construction sector. On 8 June 2020, the Government announced that alongside the resumption of Childcare Subsidy (CCS), JobKeeper will cease from 20 July for employees of a CCS approved service and for sole traders operating a child care service.

What lessons have been learned? What more could and should be done to assist business through the initial (Respond) phase of the pandemic? What can we learn and apply in for the next phase (Recover)?

Australia's approach in its initial response to the pandemic

This publication is focused on tax policy responses at the early stages of the virus: the health and economic outlooks were at their bleakest in late March and early April. It was appropriate at that time to provide lifelines to business and households, so that Australia still had the building blocks in place to take advantage of what now is expected to be a long slow recovery.

The pandemic has likely been the fastest moving crisis that policymakers in Australia and around the world have ever had to navigate. Australia leveraged from its learnings from other crises, took guidance from the OECD and reached out to other countries who were several weeks ahead of us in the pandemic timeline.

Our approach was based on a few fundamental principles:

- **Go hard with speed and solve problems on the run** ("speed over elegance")
    - The JobKeeper program was an example of this with law developed and passed at record speed, accompanied by the Treasurer's initial JobKeeper Rules. The detailed process of administering the scheme, guidance on complex issues and tweaks to the JobKeeper Rules all followed over the first few weeks of the program.
- **Use existing systems and programs to deliver support**
    - The increased payments and coronavirus supplement payments were made to recipients who were already eligible for government assistance
    - The ATO's administration machine was called into action to rollout the JobKeeper program using existing systems for employers
- **Design tax relief around existing datasets**
    - Both the cash flow boost and the JobKeeper payment relied on existing datasets – the Cashflow boost automatically triggered from PAYG Withholding data and the JobKeeper scheme leveraging heavily from the Single Touch Payroll data to check integrity and reduce fraud
- **Design solutions which are practical, pragmatic, empathetic and simple**
    - The ATO rapidly responded with novel administrative and compliance approaches and shortcuts around employee home office expenses, practical positions for employees trapped cross border, FBT concessions were a few examples of these.
- **Scalable**
    - The various measures can all be dialled up or dialled down. For example, the eligible periods for particular measures can be extended. The relevant amounts payable can be increased or decreased. Indeed, the payments under the cash flow boost as initially announced in early March were stepped up with a follow-up announcement in mid-March. We await the outcome of the Treasury review of JobKeeper, as to how that scheme may be modified prior to September, and indeed beyond September.

The Government approach wasn't perfect, wasn't precise, but our speed over elegance mantra meant that money started flowing quickly out of Treasury's coffers to support individuals and businesses in need.

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How did the nature of the crisis influence the response?

On 10 March 2020, the Prime Minister commented

> "*it was very clear that this was going to be a very significant issue that had very profound, broader, economy wide impacts, globally. Because what it does is, what this virus does is disrupts economies. Global economies, domestic economies. It's a disruptor. But it is a health disruptor, not a financial disruptor in terms of its cause. And so, it's important to keep it in perspective. This has a fixed life. This virus. It will run its course. And it's important we do things while we address this that does not impede a longer term position.*[1]

Because this was initially a health crisis, with a perceived short term rapid impact, our tax policy responses at the outset were primarily influenced by solutions put in place for natural disasters. The pandemic would impact the economy in similar ways to a bushfire or drought, in that whole areas of economic activity would suddenly cease, consumer and business confidence would be severely impacted, and people's ability to support themselves would be affected. However, both the scale of the impact and the response was exponentially larger.

Australia, like many other countries in the Asia Pacific region (such as Japan and New Zealand), regularly experiences natural disasters and already had some standard solutions in place. The social security system could again be utilised to make immediate payments to affected individuals already receiving income support.
Tax administration relief measures utilised for bushfires and drought provided some regulatory and cash flow support and could be rolled out quickly. Instead of taxpayers being eligible by postcode, these measures were extended across all taxpayer segments. These included:

- Providing extra time to pay tax debts, without incurring general interest charges (GIC)
- Remitting any penalties automatically imposed during the disaster
- Prioritising refunds
- Allowing taxpayers to varying their pay as you go (PAYG) instalments.
- Some lodgment and payment deferrals, some on a case by case basis and others on a general basis.

What was different this time?

It was evident early on that both Australia's health and economic situation was changing rapidly. Given the pandemic impacted across every geography, and every facet of the economy, the Government needed new rapid data sources in order to both monitor how the economy was going and make decisions.

This informed and influenced a number of the tax policy responses. Businesses were not given widespread lodgement concessions for their BAS and income tax returns, as the data within these would provide critical information as to which sectors of the economy were recovering or weakening throughout the pandemic stages.

Likewise, a condition of the JobKeeper registration and eligibility process, was the monthly requirement to report current and projected month turnover over the period of JobKeeper support. This disclosure would not affect entitlement, and consequently ensured that honest projections were provided to government throughout the course of the JobKeeper program, feeding much needed data to Government.

This data will also inform Treasury of the necessary tweaks that should be made to JobKeeper as part of its review into the scheme in June / July 2020.

In addition, our "normal" experience of a disaster is that the crisis comes to an end: a bushfire is extinguished, flood waters peak and a cyclone loses strength. The virus is different: so much of this is unknown and we rightly remain wary of a second-wave. So, whilst we need to proactively and confidently plan for the Recover phase, we must remain cautious that the crisis may not be over. This necessarily means that tax policy changes may not have long lead times, and may need to pivot and adapt based on the health position at the time.

Unlike normal crises, this was not localised. The health and economic effects radiated around the world at rapid speed. The lifeblood of the global economy – free and rapid movement of goods and people – was shut down or

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[1] https://www.pm.gov.au/media/qa-afr-business-summit-sydney-nsw

heavily curtailed almost overnight. Amongst countries, the pandemic brought out the good and the bad: it created some new platforms and approaches to global co-operation and information sharing and also provided a new battleground for countries to compete; for example, life-saving medical supplies. The global nature of the crisis meant that optimistic view of a quick snap back to normal, was unrealistic against the backdrop of a worldwide economic downturn, and the prospect of indefinite border closures.

The Australian responses to the initial stage of the virus

From a tax policy perspective, the immediate priorities were to respond to the escalating risks of liquidity, solvency and income support. The principal measures are listed below:

Virus phase	Tax policy objectives	Main tax policy solutions implemented
RESPOND Virus outbreak & containment & mitigation stages	Liquidity	• Tax administration – deferral of tax payments & accelerating refunds • Boosting cash flow payments for employers • Early release of superannuation • Loan guarantees to SME lenders • Various State government concessions
	Income support	• JobKeeper payments • Expanding access and relaxing conditions in respect of Jobseeker • Coronavirus supplement payments for income support recipients
	Solvency	• Temporary relaxation of insolvency laws • Code of conduct for commercial tenancies
	Stimulus	• Temporary expansion of the instant asset write-off • Introduction of a 15 month accelerated depreciation • $1 billion fund for severely-affected regions, industries and communities • Homebuilder program
	Protecting sovereignty	• Tightening of foreign investment rules

Hits and misses

Investment stimulus

In the first economic stimulus package on 12 March 2020, the government announced measures to support investment:

- The threshold for assets eligible for the Instant Asset Write-Off was increased from $30,000 to $150,000 and made available to businesses with aggregated annual turnover of less than $500 million, until 30 June 2020.
- Accelerated depreciation in the form of an immediate deduction of 50% for eligible expenditure that did not fall within the above instant asset write-off was available to businesses with aggregated annual turnover of less than $500 million until 30 June 2021.

Both of these initiatives were designed to encourage investment, to assist Australian businesses and economic growth in the short-term, and encourage a stronger economic recovery following the Coronavirus outbreak.

However, the timing – at the initial stages of the pandemic just prior to lockdown - when business confidence was low and cash flow critical, together with the limited window of opportunity to access them, meant that their effect will be blunted. The expanded instant asset write-off, which was to close at **30 June 2020**, was likely to have limited take-up. Further, if businesses were in tax losses in the June 2020 year, the timing difference benefit of the instant asset write-off would be lost.

It quickly became apparent that more was needed, and this was going to require a more direct fiscal intervention by governments. In response, the first stimulus announcement was quickly followed by "more and bigger" stimulus announcements. In addition, on 9 June, the Government announced a further six month extension to the instant asset write-off to 31 December 2020.

Boosting cash flow for employers

Another early measure was the cash flow boost. Businesses were eligible to receive the cash flow boost provided they:

- Held an ABN on 12 March 2020 and continued to be active;
- Had an aggregated annual turnover under $50 million; and
- Made eligible payments that the business is required to withhold from such as salary and wages and director fees.

The Government would provide tax-free cash flow boosts of between $20,000 and $100,000 to eligible businesses, delivered through credits in the activity statement system, when eligible businesses lodge their activity statements.

The magic here was that the process was "data-driven", and did not require any action from business. The issue of course with a data driven process is that it relies on the data. The particular rules keyed off the "aggregated" turnover of an entity, requiring the identification of connected entities and affiliates. The ATO did not and could not be expected to have full visibility of connected entities and affiliates, and hence was unable to calculate the aggregated turnover with certainty. This resulted in some businesses receiving cash flow boost payments that they were not entitled to and didn't expect. The windfall credit posed a problem as some businesses were not aware they were not eligible and could have spent the funds and for others, who were aware of a possible overpayment, there was no automated system to reverse the payment.

In addition, by going early on this measure, the Government effectively instituted two different forms of a wage subsidy scheme for businesses and provided a double up of support for some employers (especially small and medium businesses) who could qualify for both cash flow boost payments and the subsequently announced JobKeeper regime.

JobKeeper

Like many countries around the world, Australia introduced a wage subsidy scheme. Australia's JobKeeper regime had several objectives:

- To help businesses affected by the Coronavirus to cover the costs of their employees' wages, so that more employees could retain their job and continue to earn an income.
- Ensure that employees and employers maintained their connection, allowing employers to hold on to workers' talent and experience so that the subsequent economic recovery would be stronger and faster.
- To reduce the risk of fraud and to ensure money flowed through to employees, payments were to be made to the employer monthly in arrears.

Unique to Australia however was the ability to design the scheme to tie in with verifiable real time data – being the Single Touch Payroll regime. Using Single Touch Payroll and BAS statements it was possible to:

- Verify who was a direct employer
- Confirm which employees were employed at 1 March 2020, being the eligibility date for employees in the scheme
- Have a level of visibility into compliance with the wage condition through employer inputs to Single Touch Payroll.

With the payments covering in excess of 3 million employees, the JobKeeper scheme has proved to be a significant contributor to employment stability and workplace connection. This was a massive scale project required to be completed on an extraordinarily short timeline. To the credit of those involved, the policy design, law development, systems design and implementation, and rollout of the scheme were well-managed given the significant constraints.

However, there are undoubtably design issues with the scheme, which are to be expected given the scope and speed in which it was rolled out. The one size fits all subsidy meant that some eligible employees were paid more than they previously earned, other employees were not eligible and some employers qualified when perhaps the impacts of COVID-19 were not so significant. Two businesses which were essentially commercially the same, but which had adopted different legal structures could find themselves with totally different JobKeeper outcomes: one may qualify whilst the other is excluded. Policy coherence was lost in the rush (speed over elegance, again).

Whether eligibility for the regime should have been wider or narrower to cover different employers and employees remains a question. The complexity of the rules, and the upfront financing issues of employee payment prior to reimbursement have also resulted in a lower take-up of the scheme, resulting in greater numbers in the Jobseeker queues and reduced workforce participation. It is also difficult to predict whether the six month duration of the scheme is too long or too short. Further rule clarifications around the wage condition particularly in respect to monthly payers has also meant that the simple concepts on which the wage subsidy was designed have become troublesome and time consuming.

The Treasury review of the scheme in June/July will be valuable, and an important indicator of the government's thinking of the likely pace of recovery in 2021.

The problem of a Federation

One of the unique features of the Government response was the formation of a so-called National Cabinet. Pleasingly, the Prime Minister has announced the continuation of the National Cabinet to focus on job creation. Cabinet has agreed to address next-phase issues such as rural and regional Australia, skills; energy; housing; transport and infrastructure; population and migration; and health. It is expected that further aspects of the Governments JobMaker plan such as deregulation and federation reform may be added to this list.

The downside of the Federation structure was demonstrated in the plethora of State based incentives and announcements. Most States and territories were broadly enacting similar measures but did so on different timelines and with particular differences. The payroll tax implications associated with the JobKeeper scheme is a case in point: multiple announcements, different rules.

Our response compared to other jurisdictions

It is a sobering exercise reviewing the tax policy responses of other jurisdictions, as it highlights the very different circumstances facing different countries around the world, and their stage of contagion. Weaker health systems, slow responses to the virus and reduced capacity to provide fiscal and monetary policies to cushion its economic effects, have meant that very different solutions are required. Whilst Australia and others have focused their tax policy responses in the first three months to tackle the key problems of liquidity, solvency and income support, the scale of this support has varied.

Because Australia was an early mover, and was successfully able to flatten the curve, we did not have to use the tax system to prop up or support the health system. Other countries were required to institute such measures as:

- Reducing VAT rates or import duties on the supply of medical equipment and supplies
- Introducing deductibility of donations of medical supplies to healthcare institutions
- Expanding sick leave benefits or imposing sick leave requirements on employers. For instance, in New York State employers were required to provide sick leave to employees who were subjected to mandatory or precautionary orders of quarantine or isolation due to COVID-19[2]
- Providing special tax incentives to medical staff working in the front line.

Australia also anticipated that the virus would have longer term effects to our economy. Many countries around the world assumed their initial emergency measures would only be needed until about June. Australia aimed to provide emergency support through until at least September. We are already seeing countries announcing extensions to the duration of their emergency measures.

[2] https://read.oecd-ilibrary.org/view/?ref=128_128575-o6raktc0aa&title=Tax-and-Fiscal-Policy-in-Response-to-the-Coronavirus-Crisis page 18

For instance:

- Italy extended relief from tax and social contribution taxes to September[3]
- The US relaxed and broadened their wage subsidy scheme to 31 December[4]
- New Zealand extended funding for their wage subsidy scheme for a further 8 weeks[5].

As we look towards the next phase of recovery, there will be further lessons to be learned from overseas.

What next?

The Federal Government] is in the midst of a review of JobKeeper, which is to be finalised in June/July. The Treasurer has indicated that the results of this review will be communicated during the economic update on 23 July. There are only 4 remaining JobKeeper fortnights commencing after that date, 2 of which finish in August and 2 of which finish in September. It is difficult to see significant changes to the existing regime being announced and implemented from that date.

The *Coronavirus Economic Response Package (Payments and Benefits) Act 2020* defines prescribed JobKeeper period to be "the period between 1 March 2020 and 31 December 2020"[6], so can be readily extended at the stroke of the Treasurer's pen (to amend the Rules) without any need to go to Parliament. There will be a need to extend income support to those industries still subject to mitigation and containment measures (such as travel and tourism sectors). The Government is also contemplating additional industry specific measures similar to the Homebuilder package. On 4 June, the Prime Minister confirmed "I've already indicated the Government is working in the area of media and entertainment. We'll have more to say about that when we're in a position to do so."[7]

It must be acknowledged that given the scale of the economic packages and the speed in which they have been pushed out, it is inevitable that recipients have both made inadvertent error relating to eligibility and in some cases, committed fraud to gain inappropriate entitlement. The early access to superannuation scheme has already been frozen once to tighten controls. Whilst the ATO has assured many of the JobKeeper applications prior to payment, it is to be expected that many of programs recipients will be subject to compliance audits and particularly in the case of JobKeeper, documentation which supports registration and eligibility will be critical.

Australia is also currently debating what next in terms of our tax policy responses both short term (Response) and medium term (Recovery). Some tax policy responses implemented overseas could also be contemplated. For instance, other countries have:

- Introduced a loss carry back. A loss carryback is critical to convert losses and tax incentives such as the Instant Asset Write-off to cash.
    - New Zealand will allow businesses that anticipate being in a loss position for the 2020 or 2021 tax year to carry some or all of the loss back to the preceding year to enable an immediate cash refund of prior tax paid[8].
    - In the US, the CARES Act provides that losses arising in years beginning after December 31, 2017, and before January 1, 2021, will be allowed as a carryback to each of the five taxable years preceding[9]
- Extended wage subsidy schemes to a wider employer group for a longer period
    - New Zealand has extended their wage subsidy scheme to pre-income R&D start-up firms[10]
    - USA and NZ have both extended the duration of their wage subsidy schemes (as noted above).

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[3] https://www.taxathand.com/article/13690/ Italy/2020/New-law-decree-introduces-additional-tax-measures-in-response-to-COVID-19

[4] https://www.taxathand.com/article/13682/United-States/2020/House-approves-Paycheck-Protection-Program-enhancements

[5] https://www.taxathand.com/article/13670/New-Zealand/2020/Snapshot-of-recent-developments-May-2020

[6] Refer section 6 definition of "prescribed period"

[7] https://www.pm.gov.au/media/doorstop-googong-nsw-0

[8] https://www.taxathand.com/article/13496/New-Zealand/2020/Loss-carryback-rule-Fine-in-theory-but-watch-out-for-fish-hooks

[9] https://www2.deloitte.com/us/en/pages/tax/articles/covid-19-tax-policy-updates.html?nc=1

[10] https://www.taxathand.com/article/13670/New-Zealand/2020/Snapshot-of-recent-developments-May-2020

- Introduced some flexibility into timing of social security contributions
    - Italy has postponed some social security contributions to September[11]
    - Belgium has introduced an automatic deferral of social security contributions for businesses in the catering, leisure, culture, and sports sectors, and all undertakings affected by compulsory closure until December 2020[12].
    - India has reduced the statutory rate of employer and employee contributions to the provident fund from 12% to 10% of monthly pay in respect of wages payable for the months of May, June, and July 2020[13]
    - Australia is unlikely to go down this path given this is an employee entitlement. However, Australia's SGC amnesty will cease on 7 September 2020. Without an extension, many employers who had contemplated participating in the scheme will be financially unable to. Some extension to be scheme will need to be legislated to maximise employer participation.
- Allowed broader refundability of research and development (R&D) tax credits
    - The New Zealand government made amendments to its R & D tax credit regime bringing forward the broader R&D refundability proposals
    - The Australian government could consider, for example, temporarily increasing the refundability threshold for FY20 and FY21 from $20M to $50M.

Further adaptions to our tax laws will be required as we navigate through the Recovery phases.

Lessons learned

Hindsight is a wonderful thing, particularly in a once in a lifetime pandemic. But there is value in considering what lessons were learned, and appreciating what we can do by throwing co-operation, innovation and yep, a massive amount of money at a problem.

Some of the learnings we can take out of this crisis (so far) are:

- Even in a globalised, digitalised world where institutions of government struggle with issues of trust, the role of government and its fiscal response remain as important as ever
- Leadership that inspires confidence and looks beyond the current crisis is important
- Speed of response is critical to make an impact
- Flexibility of design is also critical to tailor that initial response
- Consultation is valuable, where you have time and it is done effectively (and indeed, even if you think you don't have time, consultation is still valuable)
- Parliament can move fast, and sometimes very fast
- The ATO can move fast, and sometimes very fast. ATO website guidance, regularly updated, became a new tool to get important real-time messages into the market. A wrinkle with this approach is that yesterday's web page is yesterday's news and it became difficult to track what was the new content in today's web page update: an issue that will no doubt be addressed
- The way that we have always done things isn't always the best way: there are many examples of that in government, business and the community. Perhaps the National Cabinet response is the most significant.
- Simple smarter compliance solutions such as the employee home office shortcut have value in an emergency: and actually, have value at all times
- Typically, we have designed data responses around existing laws: the tax related responses to the pandemic turned that on its head – the law was designed around existing data.

These learnings can and should play a role as we continue to navigate the Respond phase and move into the Recover phase. The next steps will be more difficult. Tax policy settings over the next one to five years will be harder and more politically charged.

Good tax policy will be necessary for Australia to survive its first recession in a generation.

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[11] https://www.taxathand.com/article/13690/Italy/2020/New-law-decree-introduces-additional-tax-measures-in-response-to-COVID-19

[12] https://www.taxathand.com/article/13532/Belgium/2020/Implications-of-COVID-19-for-international-social-security

[13] https://www.taxathand.com/article/13643/India/2020/Reduction-in-employer-and-employee-contributions-to-provident-fund-announced

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