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Tax insights
Talking tax reform: GST

GST: understanding the context of the current arrangements

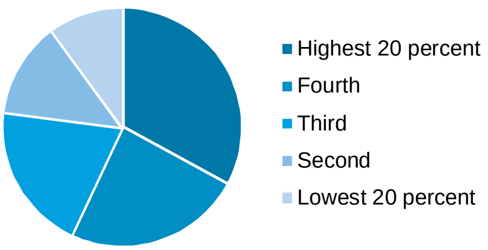
- Australia's current GST rate is 10%. The OECD average GST standard rate is 19.1%.
- Australia's GST base is not particularly broad, due to a significant portion of goods and services consumed being exempt. Added to this, our GST revenue is being adversely affected by a fall in the proportion of spending on taxable goods and services, and a corresponding increase in the proportion spent on GST-exempt goods and services such as health, education, rent and financial services.
- GST is collected by the Federal Government. However, under the Intergovernmental Agreement on Federal Financial Relations broadly all of the GST revenue is passed on to the States and Territories.
- The current political and fiscal environment is not conducive to a change in the base or rate of GST:
    - The Federal Government has indicated that it would not institute a change to the rate or base of the GST without the agreement of all the States and Territories. Many States have gone on record indicating a lack of support for changes to GST
    - If a compensation package is needed, typically this is facilitated through income tax cuts and transfer payments funded by the Federal Government. The Federal Government has indicated that at the present time "We haven't got the financial capacity to do that at the moment."

- Based on Treasury's 2014 Tax Expenditures Statement, revenue forgone in 2014-15 in respect of major categories of goods and services on which GST is not charged is estimated at:

GST free/input taxed category	Estimate revenue forgone $m
Food	6,400
Education	3,950
Financial supplies – input taxed treatment	3,550
Financial supplies – reduced input tax credits	900
Health – medical and health services	3,550
Health – residential care, community care & other care services	1,110
Child care services	1,090
Water, sewerage & drainage	1,050

- The multitude of exemptions increases complexity.
- A narrow GST does not necessarily mean it is fairer. Our current exemption system allows all taxpayers to benefit from exempt goods and services and may not be the best way to assist low income households. "In 2009-10, the top 20 per cent of highest-income households benefited from GST exemptions estimated to be, on average, 3.5 times more in absolute terms than those received by the lowest 20 per cent" per the Tax Discussion Paper.

GST revenue forgone per quintile as a proportion of total GST revenue forgone (as a result of exemptions to the GST) 2009-2010



Source: *Treasury projections from the Re: think Tax Discussion Paper March 2015*

- In early-April 2015, the Federal Government and the States and Territories agreed to amend the law to impose GST on services and intangibles supplied to Australian consumers by entities outside Australia.
- There is a view that Australia's $1,000 'low value' exemption threshold for imported goods should be lowered substantially. Work by the OECD, and recent statements by the Federal Government, suggest that a move to lower the threshold in the future might occur in conjunction with legislative changes to impose the liability to charge and remit GST on imported goods on to offshore suppliers.

Implications for business

- If you are intending on making a submission, the due date is 1 June 2015. Further consultation about the Green Paper options will happen later this year or early next year.
  - Consider strategic partnerships: Given the issues around the distributional effect of GST, many businesses are choosing to consult and/or collaborate with the NFP sector in relation to their submission
  - Consider the potential impact of any change on your supply chain and your industry competitors: Many businesses will prepare submissions on the premise of a comparative advantage or disadvantage in respect of their markets
  - Address in any submission what administrative impact a change to the base of GST would have on your business: The Government has indicated that submissions addressing red tape reduction will be favourably received
- The Federal Government has indicated that (if at all) it would not make any changes to the GST before the next election (likely to be mid to late 2016).
  - If the base or rate of GST is to change, it is unlikely that any changes to the GST would be introduced before 1 July 2017, and a later date may be chosen to provide adequate lead time for

businesses to prepare. The exception to this is likely to be imported intangibles and services, with the Federal Government signalling it wants to legislate as quickly as possible.

- Should there be a change in Government at the next federal election, the base of GST is unlikely to change in respect of food, health products, or school fees, given Labor's public policy position. It is less clear whether other ways to increase the base or an increase in the rate would be considered by the ALP should it be elected. Again, any potential changes to the GST are unlikely before 1 July 2017.
- Although several business, professional services and social welfare bodies have urged the need for a review of the GST, a lack of bi-partisan support could result in little or no action.
- A change to the GST rate or base is unlikely to fund any decrease in the corporate tax rate for the reason that most corporates do not incur GST and will not need compensation for an increase to the GST. Further, the States and Territories would have to agree to forego some of the additional GST revenue raised, a position that seems unlikely at present.

Deloitte perspectives

There is an imperative to change the tax burden from income taxes to taxes on spending. Currently work, innovation and saving are discouraged, while spending is encouraged.

Changes (if any) to the GST rate, base and administration should aim to achieve the following goals:

- Provide a larger and more sustainable source of GST revenue – as part of an overall approach aimed at ensuring that the State and Territory Governments have sufficient funding to finance the services and functions for which they are responsible
- Reduce complexity and compliance costs for suppliers, particularly small businesses. A single rate of GST, applied to the broadest range of goods and services, with minimal exemptions, would contribute substantially to achieving this.

Changes to the design of the GST would need to be accompanied by an adequate and appropriately structured compensation package for lower income households. Fair compensation would need to be structured through a combination of transfer (social security) payments and tax cuts. Such compensation would provide better targeted assistance than the current GST exemptions.

Whilst an increase in the rate of GST may be more palatable politically than removal of exemptions, the GST currently is narrow compared to its potential base, taxing less than 60% of consumption.

Removing the current exemption for food should be considered subject to an appropriate compensation package. It is less clear whether imposing GST on health and education would be appropriate. Although GST would be applied to both private and government-provided education and health services, the additional cost would likely lead to some households moving out of the private education and health systems and relying instead on free or cheaper government-provided alternatives. This shift in demand towards the public sector could erode the anticipated increase in GST revenue and involve additional demand for government provided services, and hence additional costs.

Any tax reform discussion should also provide an opportunity to amend the GST law to improve its clarity, and to revisit unimplemented measures from previous tax reviews such as:

- Making greater use of GST-free treatment or reverse charging of B2B transactions
- Development of an alternative method of taxing domestic consumption of financial services

A lowering of the $1,000 'low value' exemption threshold for imported goods continues to be problematic, due to the costs of collection and enforcement. There are indications that the OECD and the Federal Government are coming closer to a solution. Any revenue increases on offer here are likely to be relatively small, however there should be additional benefits in terms of improvements in competition and the integrity of the GST system over time.

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