NSW Young Liberal Movement Submission to the Federal Financial Relations Review

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Prepared by members of the NSW Young Liberal Policy Committee
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Mr David Thodey AO
Chair, Federal Financial Relations Review

Re: Federal Financial Relations Review

Dear Mr Thodey,

Please find attached a submission prepared by the Policy Committee of the NSW Young Liberals for the NSW Federal Financial Relations Review.

As a Movement, we are concerned about equity for the next generation. Our generation will have to inherit the consequences of a lack of will by governments to undertake vital tax reform. If nothing changes, our generation will be saddled with higher taxes and more debt. We will be unable to sustainably pay for the public services our society relies on.

The NSW Young Liberals believe that substantial tax reform, which can only be achieved with the States and the Commonwealth working together, is necessary to ensure that NSW can continue to deliver essential services and infrastructure.

It is our hope that any options considered by the Review will consider the pressures that the young people of NSW face such as housing affordability and youth unemployment.

Therefore, we submit that taxes which particularly burden young people, like stamp duty and payroll tax, should be abolished. Stamp duty unfairly prices young people out of the market. Payroll tax prices young people out of the labour market and dampens wage growth.

These taxes should be replaced by fairer and more efficient taxes which minimise distortion of economic decision making and lead to a fairer distribution of the tax burden. Any new tax should be as low as possible. Any reform should ensure the overall tax burden is lower.

We believe that good tax reform will open doors to greater prosperity in this State. The abolition of unfair taxes on young people will give young people a fair go to pursue more job opportunities and reap the benefits of long term security that come from establishing a foothold in the housing market.

We thank the Panel for considering our views.

We would be happy to respond to the Panel should you have any further questions. If we can be of further assistance, Policy Vice President Hugo Robinson can be contacted

Sincerely,

Chaneg Torres
President
Young Liberal Movement of Australia
(NSW Division)

Hugo Robinson
Vice President, Policy
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Introduction

Current Australian tax laws diminish the ability of young Australians to find jobs and accumulate assets. From stamp duty, making it more difficult for individuals to purchase homes, to payroll tax reducing the incentive for employers to hire new workers, it is time for the State and Federal Governments to take tax reform seriously to ensure that the next generation is given a fair go and not burdened by the impacts of Australia's current tax laws.

Young people already carry many financial burdens. Rent, student debt, transport, costs associated with studies and work; all of these payments create significant cost of living pressures on the lives of young Australians trying to save.

For young people trying to establish themselves and struggling to save, stamp duty adds a significant cost barrier, making it difficult for young people to break into the housing market for the first time. It also disincentivises investment which leads to a drag on the economy.

Additionally, payroll tax reduces incentives for an employer to hire new people, making it harder for young people to obtain casual work through university as well as acquiring a full-time job once they have left. This in turn will prevent them from being able to accumulate savings or spend more of their hard-earned money on items that are of interest to them, leading to less economic growth.

By examining the current tax law and looking for avenues in which efficiency of the tax system can be increased, there is evidence demonstrating that tax reform is possible and has the potential to bring about significant benefits to young Australians.

This submission will consider the impacts that the current tax system is having on young Australians and suggest new ways for our State and Federal Government to order its tax arrangements.

1. Phasing Out Stamp Duty and Replacing with a Broad Based Land Tax

Taxation in NSW is ripe for structural reform. The first recommendation of this submission is that the NSW Government begin to work towards ultimately phasing out stamp duty and sourcing the lost revenue from a broad-based land tax.

Stamp duty raised $6.9 billion this year, constituting 21.6 percent of 2019-2020 NSW tax revenue. NSW has a troubling over-dependence on stamp duty, which fluctuates with the ever-changing property market.

Stamp duty is an unreliable and inefficient tax. It stifles mobility in the property market, leading to a more sluggish economy. Stamp duty is also subject to the volatility of the property market, and so is not a reliable source of revenue for the state. The NSW Productivity Commission found that stamp duty cost the economy $2.35 for every collected dollar, compared to only 16c for land tax. Stamp duty is responsible for damaging economic and social impacts on the people of NSW.

One of the most adverse effects of stamp duty is how it disproportionately affects young people. Housing affordability is a big challenge faced by young people today. Stamp duty prevents home ownership, and only exacerbates inequality between an older asset-rich generation and a younger asset-poor generation.

With the median price of a Sydney home at $1 million, the $40,000 in stamp duty plus the need for a deposit prevents young people from entering the property market. To the Government's credit, efforts have been made to assist people in buying their first homes, such as through the First Homeowner Grant scheme and stamp duty concessions for first home buyers. However, these initiatives are ultimately band-aids over a deeper issue that demands structural reform.

Stamp duty needs to be replaced by a more sustainable, and reliable tax. And there is a viable alternative in land tax.

The 2019 Henry Tax Review supported the implementation of a broad-based land tax. Land tax already exists in NSW. From 2019-20 land tax will raise $4.5 billion in revenue, or 14.3 percent of the NSW taxation mix. This stream of revenue is impeded by the current exemptions which apply to land tax, primarily driven by the existence of stamp duty. Further, since owner occupied homes are exempt from land tax, young people end up paying higher rents due to investment properties bearing the burden of land tax.

Unlike stamp duty, land tax has the support of most economists and offers a stable, progressive means of raising revenue. This stability is due to the fact that, unlike stamp duty, land tax's base is land which is immobile. Therefore, the supply of land is essentially fixed, ensuring that land tax will be paid regardless of how developed it is.

The property market in NSW is undergoing a period of volatility, which is likely to worsen due to global economic conditions. This has a run-on effect on stamp duty, as it is effectively indexed to the property market. By contrast, a recent report by Prosper Australia has indicated that a transition to land taxation could, regardless of market conditions, be worth as much as $170 billion to the economy. This transition has the support of Productivity Commission chairman Michael Brennan.

Additionally, there are social benefits to adopting a land tax. Unlike stamp duty, land tax does not hinder market mobility, nor does it incentivise rampant speculation. This should increase the supply stock of housing, as it encourages landowners to develop vacant/underused land or sell it on, avoiding the distortion of market outcomes in the process. This effect has been seen in Harrisburg, Pennsylvania, where land tax reduced the number of vacant structures from around 4,200 to fewer than 500.

Land tax has progressive effects, as it focuses on owners of valuable land who tend to be wealthy and does not allow the tax burden to be passed down. Furthermore, the threat of tax evasion is effectively nullified as, unlike other capital assets, land cannot be concealed or moved overseas, and is publicly registered.

Stamp duty is an archaic, inefficient and unethical tax. Land tax provides a stable and efficient alternative, offering a solid revenue base for the future of NSW.

2. Abolishing Payroll Tax

The widespread imposition of payroll tax provides numerous barriers to long-term, meaningful employment for young people insofar as it creates disincentives to hire new employees.

Currently, payroll tax seeks to work as a form of progressive taxation to only charge larger businesses. However, by imposing costs on employers to hire additional workers, a payroll tax renders expansion past a certain threshold unprofitable and in turn undesirable. As a result, if faced with the decision to increase the scope of operation or to maintain a level below that to be met with the tax, a company may be inclined to follow the latter strategy.

This is detrimental to young people as they are likely to be seeking employment in these firms. Young people also experience reduced wages to compensate for the tax. If there is consequently decreased demand in the labour market for young employees, levels of youth unemployment, alongside underemployment, are certain to rise. In turn, reliance on the welfare system may similarly rise.

Thus, we would suggest that in order to combat the adverse implications young people are faced with, the payroll tax should either be abolished in its entirety, or the threshold for its operation be increased so as to apply to corporations that would unlikely be deterred from incurring it due to their scale of operations.

In 2018, NSW Treasurer and NSW Commissioner for Productivity asked PwC to create a detailed report on the impacts of payroll tax on NSW businesses and recommendations to improve productivity. The report outlines that the current attitude towards payroll tax is a sense of confusion and clutter for business to manage their finance administration. Currently, 190 full-time employees (FTE) are used to perform the administration on behalf of the government, however very limited staff are available to educate business on how to navigate through payroll tax.

3. Broadening the Tax Base: GST

Australia's tax system is heavily reliant on inefficient taxes on profits, income and capital gains. The OECD has ranked Australia the second highest in taxes from these sources. Additionally, Australia is ranked 34th out of 36 counties in the share of the revenue gained from a VAT. Australia only raises 13 percent of its revenue from a GST, compared to the OECD average of 20 percent.

Broadening the base of GST, by including items such as fresh food, medical treatment, and school fees, and increasing the rate of the GST would allow for cuts in other, more inefficient taxes.

Additionally, it would reduce the fiscal imbalance between the states and the Commonwealth by enhancing the states' financial independence. The OECD, in its 2019 Reform priorities, argues that Australia should broaden and increase the GST. CEDA, the Tax Institute, the Grattan Institute, and the Australia Institute have all argued for this stance as well. Several prominent Australian economists, including Chris Richardson, Ken Henry and Richard Highfield, have argued for increasing the rate, and broadening the base.

We submit that any increase in the rate and broadening of the GST's application must coincide with the lowering or abolition of other inefficient taxes

4. **Digital Services Tax**

The modern, globalised tax system has been unable to effectively tax technology companies. In 2018, Google and Facebook collectively generated $4.8 billion in revenues in Australia, yet they only paid $38.3 million in corporate tax. The international tax framework is outdated in that it allocates taxing rights based on the location of physical assets and labour. Technological advances mean digital businesses can 'have a significant economic presence in on jurisdiction, while the majority of its profit-generating assets and labour can be located in a different jurisdiction.'

The OECD Task Force on the Digital Economy is scheduled to release a Final Report containing long-term solutions for taxing the digital economy in 2020. However, considering the inherent complexities surrounding the implementation of any global regime, 'an interim digital services tax may be warranted given the likelihood that no long-term global solution is in sight.'

Implementing an interim digital services tax presents a significant opportunity to broaden the tax base. France's Digital Services Tax imposes a 3 percent tax on the turnover large technology companies make on digital services (advertising, resale of personal data etc) and is estimated to raise around €500 million a year. Significantly, France's Digital Services Tax applies only to companies that have worldwide revenue of €750 million a year and generates more than €25 million from French customers. The narrow scope of application means that only around 30 companies will be affected, protecting smaller technology companies as well as large companies with small domestic presence. A Digital Services Tax is scheduled to be introduced in UK, Italy and Spain.

Digital products provide huge benefits to the economy, with the younger generation of workers benefiting significantly from technological innovations. Yet it is clear that the current taxation system does not adequately tax large technology companies. Overall, having a digital services tax can increase the tax base and ensure that the revenues generated by largely overseas technology companies flow back into the Australian economy. It could also lead to opportunities to lower taxes in other areas.

Conclusion

Taxation in NSW as it currently stands is not sustainable and is to the detriment of young people. While we recognise that tax reform generally incurs serious political scrutiny, responsible governance demands that we re-evaluate how this state will raise its revenue. This submission calls for a move towards fairer, more efficient and lower taxation. A move from stamp duty to land tax, the rolling back of payroll tax, the broadening of the GST and the introduction of a digital services tax are the four recommendations made in this submission. We hope these recommendations will be considered by the Panel.