Howard aims for a corporate tax bonanza in Australia

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16 August 1999

It is indicative of the financial pressure felt by governments around the world that the Howard government in Australia is scurrying to introduce sweeping taxation changes by July 1 next year to further boost corporate coffers and attract major investors.

Prime Minister Howard and Treasurer Peter Costello last week indicated that business can look forward to a triple bonanza—the reduction of the top company tax rate from 36 to 30 percent, the halving of the Capital Gains Tax and the retention of accelerated depreciation allowances.

No official figure has been given, but investors will benefit by tens of billions of dollars per year. By best estimates, the company tax cut alone will be worth $10 billion annually, equal to the total amount that the federal and state governments spend on public hospitals.

Only last month, after weeks of political turmoil, the government—propped up by the Australian Democrats—finalised a package to cut income tax for wealthy people by up to $60 a week per individual and introduce a 10 percent consumption tax (Goods and Services Tax—GST) that falls most heavily on low-income earners.

Before the ink was even dry on the agreement with the Democrats, big business and the media owners had renewed their demands for drastic cuts to business taxation. It mattered little that the government had not received the report of its own Review of Business Taxation, set up a year earlier under prominent businessman John Ralph.

"Gains tax to be halved—PM to signal lure to investors" proclaimed the banner headline in Rupert Murdoch's national broadsheet, the *Australian,* on July 14. The newspaper confidently predicted that Prime Minister Howard would promise lucrative tax cuts when he addressed a business audience in New York City the following day.

Howard's speech did not disappoint. He committed his government to a more "investor-friendly" tax system, saying existing arrangements were a serious barrier to investment. His remarks showed the extent to which such cuts are today dictated by the global financial markets.

Addressing an Australian government-sponsored conference to promote Sydney as a regional financial centre, Howard said the results of his government's bid to overhaul business taxes would determine how the national economy performed in the future.

Tax cuts had to compete with those already implemented in the US. "I know that in a globalised world, you really have to have a tax system that, as far as possible, makes the choice between an investment in the United States and an investment in Australia neutral." Howard identified US pension funds as a special target, saying one option was to make it easier for them to secure capital gains tax exemptions in Australia.

Moreover, Howard offered hope that the official opposition parties—the Labor Party and the Australian Democrats—would ensure the passage of legislation through parliament. "I am optimistic ... we'll be able to put forward some sensible reforms in the corporate and capital gains tax area and win the support of the opposition parties."

Ralph handed his report to the government on August 2. Federal cabinet is not expected to issue its formal response for several weeks yet, partly because serious infighting is taking place over which sections of business should benefit the most, but the general shape of the corporate handouts has already been made known through numerous media leaks.

The first feature is the 30 percent top company tax rate; something to which Treasurer Costello publicly committed himself before the Ralph review began. Just 15 years ago, the rate was 49 percent. One of Costello's Labor Party predecessors, former treasurer and prime minister Paul Keating, presided over the reduction from 49 to 36 percent, estimated to be worth $17 billion annually.

The second major plank is the halving of the capital gains tax rate. For those earning above $75,000 a year, the tax they pay on profits from share transactions or other asset sales will tumble from 47 to 23.5 percent. In order to attract speculative "venture" capital from the US, the reduction will apply to all capital gains, with no discrimination in favour of those investing in productive capacity.

A host of other business concessions are expected, including lower taxes on profits from overseas subsidiaries, and special capital gains tax exemptions for small businesses.

Finally, the government last Thursday dropped suggestions that it would scrap accelerated depreciation allowances to compensate for the cost of the company tax cut. Friday's

Financial Review described the government's reversal as "a major win for business".

This aspect of the proposed tax blueprint had generated severe conflicts within ruling circles. Sections of business that stood to lose most from the abolition of the allowances—capital-intensive operators in mining, agriculture and manufacturing—had bluntly threatened the government in recent weeks.

The Minerals Council, representing most major mining companies, had warned that the loss of accelerated depreciation would cripple exploration spending and mean a "dramatic loss of competitiveness" for the mining industry. The National Farmers Federation, speaking for large agribusinesses, had been highly critical as well.

These threats inflamed divisions inside the coalition government. Deputy Prime Minister John Anderson, the leader of the junior partner, the rural-based National Party, told a Queensland state conference of his party that concessions on company and capital gains taxes should not be at the expense of changes "detrimental to the interests of our traditional industries".

Within the majority partner, the Liberal Party, rifts erupted between those, like Costello, who champion the ever-strengthening interests of Sydney-based finance capital—the banks, insurance companies and share traders—and other senior ministers associated with manufacturing, mining and agribusiness, traditionally centred in Melbourne.

According to the *Financial Review*, a bloc of cabinet ministers, including Anderson, Defence Minister John Moore and Industry Minister Nick Minchin, insisted that the depreciation tax incentives remain.

In order to avoid a public confrontation, Costello and Howard foreshadowed a series of "integrity measures" to supposedly close off certain capital gains tax loopholes to partly cover the cost of the company tax cut to 30 percent.

In reality, such anti-avoidance measures are highly unlikely to produce any revenue. Large companies and rich individuals will simply find new loopholes. As the *Financial Review* noted on Friday: "The move to broaden the CGT [Capital Gains Tax] base will require high-wealth individuals to restructure their business arrangements, according to well-placed sources."

The four major banks have already calculated the profit gains they expect various segments of big business to enjoy as a result of the tax changes. Mining production will rise by 6.2 percent; wholesale trade by 4.1 percent, manufacturing 3.7 percent and agriculture 2.6 percent, according to modelling done for the banks by Econtech.

The chief executives of the four banks—National Australia Bank chief executive Frank Cicutto, Westpac chief David Morgan, ANZ Bank boss John McFarlane and the Commonwealth Bank's David Murray—presented the estimates to Howard at a special meeting with the Prime Minister last Thursday.

Noticeably, the *Financial Review* did not disclose the predicted for the banks and other financial institutions. It merely noted that, "the finance and insurance industry are the big winners, paying less tax as a proportion of profits".

Other commentators have lashed the government for not moving fast or far enough to please the finance sector. Among them is former Liberal Party leader John Hewson, a merchant banker. A columnist in the *Financial Review*, he lambasted the government's insistence that the Ralph report's recommendations had to be "revenue-neutral". Hewson said the overall level of corporate tax simply had to be lowered if the government hoped to achieve "its desire of developing Sydney as a global or regional financial centre".

As for the Labor Party, its leaders have solidarised themselves with such sentiments. They are anxious to prove that their big business credentials are just as good as the government's. Shadow Treasurer Simon Crean has written to his opposite number, Costello, asking for a copy of the Ralph report and for talks on striking a deal to get its recommendations through parliament. "Labor is willing to identify the common ground, commit to genuine negotiation on areas of disagreement and support rapid passage of legislation," Crean said last Thursday.

One additional factor driving the Labor leaders is their desire to capture the electoral support of what they describe as the "aspirational layers" of society—roughly the top 20 percent of income earners, who stand to gain enormously from the restructuring of the taxation system. Noting that the Labor Party would not oppose the business tax changes—in contrast to its stated opposition to the Goods and Services Tax—the *Financial Review* observed that, "Labor now wants to appeal more broadly to middle-class aspirations".

The tax changes will deepen the social polarisation taking place in Australia. Recent figures from the Bureau of Statistics show that the highest earning 20 percent now took home 48.3 percent of the country's income in 1998, up from 47.5 percent a year earlier. This "aspirational layer" is increasingly living in a different world to ordinary people. Sixty percent of people are earning less than $613 a week and the bottom 20 percent have only 3.8 percent of the income.